for industry blahs

ways to improve profitability through cost efficiencies, sources like John McNamara and John Kennedy, exec vp and chairman of Alco Standard, and Bill Bindley, president of Bindley Western, also say they believe that the severe price differentials are declining somewhat in intensity and numbers. The differentials contributed to illegal diversion and to the formation of retail buying groups as protection against buying inequities.

As a result of the decline, these sources speculate that at some point wholesalers will be able to operate more efficiently and without having to compete "just on the basis of price."

"Some manufacturers have implemented policies that would preclude favorable pricing. I hope that this is a trend," Bindley said. "I wouldn't call it a trend yet myself, but I would call it steps in the right direction."

Other wholesalers are encouraged by the Justice Department's latest opinion statement on diversion, indicating that the practice of buying pharmaceuticals from secondary sources is not illegal per se.

The industry's fear of possible illegalities in dealing with secondary sources had caused many wholesalers to stop buying diverted goods. Many sources said this practice had hurt the bottom line.

'There have been a number of wholesalers who have eliminated secondary source buying because of problems of diversion, and that has had a negative impact on margins.'

—Mel Whitmire
president,
Amfac

"There is no doubt that we did hurt our profit margins when we stopped buying from secondary sources about a year ago," said Bergen's Jack Fay.

"There have been a number of wholesalers who have eliminated secondary source buying because of problems of diversion, and that has had a negative impact on margins," said Amfac's Whitmire. "The result is that profits are not as good as they were in prior years."

Now that Justice has issued a clarifying statement on the status of secondary source suppliers, most wholesalers anticipate a shift back to this avenue of supply.

Diminished inflation

For most wholesalers and analysts who follow the wholesale industry, the one problem that does not seem likely to disappear soon is dwindling inflation.

Tauscher at FoxMeyer notes that pharmaceutical inflation, which had been running at an 8%-10% rate for most of 1985 and early 1986, has declined in the last six months. He thinks the rate will continue to drop.

Whitmire describes the lack of inflation as "the major issue facing the industry today."

"In the past," Whitmire said, "inflation has been the largest contributor to profits. We haven't had it in 1985 or 1986, and personally, I don't think that will change that much next year."

At McKesson Drug, president Joe Polastri agrees. "When you don't have high inflation, you don't have a cushion to increase your profitability. You're carrying a large inventory, and when prices go up, that tends to pick margins up. But when there is no inflation, that tends to reduce margins."

"If you cut inflation out of this business," Tauscher said, "half of your profitability also goes."

At Drexel Burnham Lambert in New York, industry analyst Joel Liffman is not predicting any immediate solutions to the inflation problem. Liffman thinks the industry will have to face diminished inflation, hovering around a 5%-6% rate, for at least the next couple of years.

That will mean, of course, slower revenue growth for the industry and a proportionately slower growth in profits.

But although Liffman calls diminished inflation "the industry's most critical issue," he predicts the industry will be able to offset most of its negative effects by evolving, through continued consolidation, beyond the current and familiar competitive phase that has resulted in bidding wars and margin erosion.

Acquisions

In the view of most industry sources, the consolidation that the industry has been undergoing for the past few years is in itself a strong antidote to diminishing inflation.

In the last two years, there have been at least 17 acquisitions of wholesale drug companies by members of the top 10 companies.

Fifteen of the 17 major 1985-1986 acquisitions were made by the top four wholesalers.

The result is that, by most industry estimates, the top four companies by year-end 1986 will account for about

Continued on page 16

Highest volume drug wholesalers

Company	F.Y. ending	Est. drug wholesale sales* (in millions)	1-year change
1. McKesson Drug *(San Francisco)*	3/31/87	$4,500	10%
2. Bergen Brunswig *(Los Angeles)*	8/31/86	2,400	25
3. Alco Health Services *(Valley Forge, Pa.)*	9/30/86	1,300	35
4. FoxMeyer *(Denver)*	3/31/87	1,300	60
5. Harris Wholesalers *(Solon, Ohio)*	4/30/87	941	22
6. Bindley Western *(Indianapolis)*	12/31/86	705	11
7. Amfac Drug Supply *(Burlingame, Calif.)*	12/31/86	543	12
8. Cardinal Drug Wholesale *(Dublin, Ohio)*	3/31/87	360	83
9. Ketchum Distributors *(Newington, Conn.)*	4/30/87	335	10
10. Humiston-Keeling *(Chicago)*	5/1/87	$318	10%
11. Durr Fillauer *(Montgomery, Ala.)*	12/31/86	266	25
12. Owens & Minor *(Montgomery, Ala.)*	12/31/86	217	24
13. Louis Zahn Drug Co. *(Melrose Park, Ill.)*	12/31/86	190	15
14. Northwestern Drug *(Auburn, Wash.)*	1/31/87	187	10
15. Drug Guild Distributors *(Secaucus, N.J.)*	7/31/86	150	12
16. Twin City Wholesalers *(Minneapolis)*	4/30/87	150	27
Total		**$13,862**	

*Excludes sales of hospital surgical supplies, mass merchandise services, etc.

Source: *Drug Store News* survey and company annual reports

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Leaders to garner 75% of sales

The bigger wholesalers like McKesson and Bergen Brunswig are consolidating their distribution centers to handle the customer base more economically.

Continued from page 15

60% of total drug wholesaling sales, while the top 10 will account for about 75%.

As most analysts and wholesalers point out, consolidation will foster economies of scale and higher profits.

Many smaller and regional wholesalers say the high-volume wholesalers already have the edge in systems that make them more efficient and are therefore more capable of providing value-added services to their customers.

In turn, the success of high-volume wholesalers—their ability to engage in drawn-out pricing wars or to cut margins to the bone to win bids for hospital contracts and other low-margin, high-volume business—is forcing many small and regional wholesalers to consider selling out.

In California, Mary L. Yost, who follows the wholesale drug industry for San Francisco-based Baldwin Capital Partners, predicts that in five years, the top six wholesalers—McKesson, Bergen, FoxMeyer, Alco, Amfac and Harris—will account for approximately 90% of all industry sales.

Wholesalers like Alco's McNamara think her prediction is too extreme and that the top five or six will probably level off to between 75% and 80% of all sales. FoxMeyer's Tauscher, on the other hand, agrees with the prediction. He thinks it will happen sooner, perhaps within "two to three years."

"It could happen," agrees Laurie DuBow, president of Lawrence Pharmaceuticals, which was itself acquired by FoxMeyer earlier this year.

"In five years, we'll probably be a $20 billion industry, and I can imagine that $17 billion a year in sales or more could be done by just the top five," said DuBow.

Most wholesalers are reluctant to speculate that the approximately 85 companies still privately held may not have much of a future left. Most prefer to agree with DuBow, who argues that there will always be a place for strong regional and local wholesalers who can provide high service levels and courteous treatment to customers.

But these same sources also acknowledge that, excluding Harris, there are only a handful of companies left that are

Continued on page 18

> *'In five years, we'll probably be a $20 billion industry, and I can imagine that $17 billion a year in sales or more could be done by just the top five.'*
>
> **—Laurie DuBow**
> president,
> Lawrence Pharmaceuticals

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Drug wholesaler customer sales mix

Customers	1978	1982	1983	1984	1985
Independent drug stores	62.41%	56.10%	54.51%	53.45%	50.01%
Chain drug stores direct	20.61	22.30	20.83	19.66	23.16
Hospitals	10.91	15.64	17.43	18.61	19.47
Chain warehouses	3.77	3.41	4.22	4.74	4.16
Mass merchandisers/ food stores	1.50	1.55	2.03	2.26	1.96
Clinics, nursing homes, etc.	0.82	1.00	0.98	1.28	1.24

Source: NWDA 1985 Operating Survey

Drug wholesalers: five-year sales growth
(In billions)

	1981	1982	1983	1984	1985	1986 est.*
Dollar sales	$8.60	$10.20	$11.90	$12.52	$14.32	$16.5
% change vs. prior yr. (current dollars)	+12.4%	+18.6%	+16.70%	+12.80%	+14.80%	15%
% change adjusted for product price changes/ inflation (constant dollars)	n.a.	n.a.	+ 9.72	+ 4.84	+ 8.65	—

*Drexel Burnham Lambert
Source: NWDA 1985 Operating Survey

Wholesale drug industry stubs financial toes

It wasn't the best of years, financially speaking, for the drug wholesaling industry.

Although 1985 sales in current dollars were up nearly 15% to $14.8 billion, overall profitability, as measured by such key indicators as net profit margins and return on total assets, dropped significantly.

According to the National Wholesale Druggists' Association's (NWDA) 1985 Operating Survey, on a composite average basis, the aftertax net profits to net worth ratio fell by a fifth to 13.07%; and the aftertax net to sales ratio was down 17% to 1.47%.

What happened to cause the decline? NWDA says noninflation and lower interest rates reduced the industry's need to engage in heavy financial leveraging. Moreover, wholesalers were unable to cut "operating expenses that could offset the continuing decline in gross profit margins."

"In the past," NWDA financial analysts point out, "the wholesale drug industry has been able to compensate for its declining net profit margins by increasing asset turns." But the turnover rate dropped 6% to 3.88 turns in 1985.

More serious problem

However, the more serious problem for the industry is that return on total assets in 1985 suffered a decline, deteriorating to 6.05% in 1985 from 7.30% in 1984. NWDA said this was the industry's lowest performance in this measure since 1979. The decline was caused by drops in both net profit margins and total asset turnover.

At the same time, the industry's average collection period increased slightly, from 26.7 days in 1984 to 27.1 days in 1985. Similarly, the average days' sales in inventory increased slightly from 50.0 days to 50.7 days.

Strong in comparison

NWDA points out that even though the industry's profitability performance this year was disappointing compared with what the industry has achieved in the past five years, it is still a relatively strong performance.

According to NWDA, compared to other wholesale distribution industries, a 13.1% return on net worth (RONW) is an "excellent performance." NWDA said the 1985 composite average for drug wholesalers is in the "upper quartile of all U.S. wholesale firms." NWDA also said that most broad surveys of RONW among U.S. firms showed a decline during 1985.

Sales gains for the industry were also strong. Growth in constant dollars was up 8.65% in 1985, compared to just a 4.8% increase in 1984.

Much of the sales gain can be attributed to the industry's expansion into new markets, both in terms of customer trade and product mix.

But as the NWDA points out, this strategy, while it added more dollars to sales and net profits, also resulted in the reductions in gross margins. That contributed in turn to the reductions in the per cent of net profit to sales, the return on total assets and the return on net worth.

NWDA conclusion

In summarizing its findings, the NWDA concluded that from this point on it is "unlikely that the industry can depend on further improvements in asset management to offset declines in net profit margins."

However, if the industry is to be able to maintain reasonable profitability levels, the NWDA acknowledged that "net profit margins will have to be stabilized" somehow.

But NWDA also conceded that at a time when many companies are struggling to defend and increase their market share as well as to enter and dominate emerging markets, stabilizing margins is going to be "difficult."

Drug wholesalers: product sales mix

Product line	1978	1982	1983	1984	1985
Pharmaceuticals	62.79%	65.34%	68.16%	71.73%	75.75%
Proprietary	17.93	15.53	14.94	13.15	12.50
Toiletry	10.04	9.51	9.14	8.42	5.92
Sundry	7.91	7.89	6.26	4.96	3.75
*DME/HHC	—	—	—	—	0.57
Other	1.33	1.73	1.50	1.76	1.52

*Prior to 1985, sales of durable medical equipment and home health care items were not tracked separately.
Source: NWDA 1985 Operating Survey

Drug wholesale industry profitability declined in 1985
(FIFO results, based on compositive averages)

Indicators	1982	1983	1984	1985
Return on net worth	18.10%	16.50%	16.40%	13.10%
Return on total assets	7.66	7.17	7.30	6.05
Net profit margin	1.95	1.75	1.78	1.47
Total asset turnover	3.94	4.11	4.13	3.88
Gross profit margins	11.00	10.16	9.74	8.86

Source: NWDA 1985 Operating Survey

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No fast relief for 'digestion' ills

Major drug wholesale acquisitions 1985-86

Company	Acquisition	Est. sales of acquired company (in millions)	Date of acquisition
McKesson	Johnson Drug (Tampa, Fla.)	$110	1 Q '85
	Spectro Industries (Jenkintown, Pa.)	$450	2 Q '85
	S-P Drug (Brooklyn, N.Y.)	$165	3 Q '85
Bergen Brunswig	Davis Companies (Denver, Colo.)	$110	2 Q '85
	Synergex Corp. (Fresno, Calif.)	$330	3 Q '85
	Berry Wholesalers (Antioch, Tenn.)	$ 50	1 Q '86
	Los Angeles Drug (Rosemead, Calif.)	$160	2 Q '86
	Southwestern Drug (Dallas, Tex.)	$150	2 Q '86
FoxMeyer (Merged with National Intergroup 1Q '86)	McPike (Kansas City)	$209	2 Q '85
	Ben Franklin	$410	1 Q '86
	Lawrence Pharmaceuticals (Jacksonville, Fla.)	$200	3 Q '86
Alco Health Services	Valdosta Drug (Valdosta, Ga.)	$ 22	4 Q '85
	Meyers & Co. (Tiffin, Ohio)	$100	4 Q '86
	L. S. DuBois Son & Co. (Paducah, Ky.)	$100	3 Q '86
	Pennington Drug (Joplin, Mo.)	$ 17	3 Q '86
	Mississippi Drug (Jackson, Miss.)	$ 49	4 Q '86
Cardinal Distributors	John L. Thompson Sons & Co. (Troy, N.Y.)	$ 20	1 Q '86
	James W. Daly (Lynfield, Mass.)	$140	2 Q '86

Source: *Drug Store News* survey

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doing over $50 million a year in sales and only two or three like Humiston-Keeling and Zahn doing several hundred million.

Zahn, in fact, may be the last privately held wholesaler generating close to $200 million from a single distribution center.

Sooner or later, say most sources, these remaining small companies will sell out. Only a handful will be left to serve a geographic region or a market segment where a niche is still available.

Digestion problems

In the meantime, the "digestion problems" that acquiring companies inevitably experience are taking their toll on industry profitability.

At Bergen Brunswig, management says the main reason earnings declined in 1986 (Bergen's first decline and first quarterly loss in eight years) was the difficulty of digesting approximately one billion in sales that Bergen picked up through acquisitions over the past two years.

Inflation was part of the problem, said exec vp Jack Fay, but Bergen's slowdown came primarily because the company "moved faster than we planned in acquiring new companies." Fay said Bergen is currently experiencing heavy debt and excess facilities, but "the basic problem we have is one of digestion."

> *'In a competitive market, you take the opportunity to acquire market share where and when it presents itself. Then these acquisitions take a while to sort out.'*
>
> **—Jack Fay**
> exec vp,
> Bergen Brunswig

"In the past two years, we proceeded at a much faster pace than we had planned, and that's because the industry is starting to get to the end in terms of eligible companies.

"In a competitive market, you take the opportunity to acquire market share where and when it presents itself. Then these acquisitions take a while to sort out."

"Bergen has to consolidate its new acquisitions into its existing facilities," said Drexel's Liffman. "There's an opportunity for them to realize substantial savings and economies as they accomplish that. The same is true for most of the top volume wholesalers, including FoxMeyer, Alco and McKesson."

Future outlook

Analysts Liffman and Yost as well as some of the chief executives of high-volume companies believe the progression into an oligarchy will gradually stabilize profitability.

"Usually with an oligarchy," said Tauscher, "you

Continued on page 19

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'86 ANNUAL WHOLESALER REPORT

How far can efficiency go?

Continued from page 18

don't have price wars unless you have a real perceived cost leader, and there aren't any real perceived cost leaders in the top four or five."

"Once you have four or five guys controlling 90% of the industry sales, you have less to gain from battles for market share increments, and that could lessen the need for competitive bidding or price wars.

"That could mean that in two or three years, margins will stabilize in this industry, and competition will be based not so much on price, but on the types of services that are being offered customers."

Gene Vykukal, vice chairman of Southwestern Drug and chairman of the National Wholesale Druggist's Association, agrees with Tauscher, but also thinks that changes have to be made now if that stability is to be achieved by 1987 or earlier.

"Some of the corrective measures are being taken now," he said, "but they only began at the end of last year, and I'm not sure if there's enough happening to help 1986's profitability.

"But in 1987, I think we'll see improvements, and it's for a variety of reasons: changes that are being worked out now to improve the charge-back systems, the possible passage of legislation that will clarify the legitimate role of secondary suppliers in drug wholesaling, the elimination of inequitable price differentials for different classes of trade, the digesting of all the major acquisitions that have occurred in our industry, and the continuation of the consolidation phase and the maximizing of the efficiencies that acquisitions have made possible."

Vykukal, however, also worries that, as the 1985 results from NWDA's operating survey show, "the cost of goods sold is once again outpacing the industry's ability to become more efficient."

Like most wholesalers, he questions "how much further we can go in improving profits through operational efficiencies alone."

"In the past," said Fox-Meyer's Tauscher, "we as wholesalers were able to operate by getting back in cost reductions whatever we gave away in price to get the business, but now we've reached a point where there isn't much more we can get back in cost reductions. Maybe there's about 25% of costs left that can be reduced by new efficiencies. That's it.

"From now on, most improvements in profits will have to come either from margins or from inflation, and with inflation running low and beginning to look like it may go lower, the improvements will have to come from margins."

Are more operational cost savings possible?

Some wholesalers say industry can always count on technology to help them do better.

"You can always do better at managing your operations," said Seth Harris. "You can particularly do a lot better as you get larger. A small change in one area can produce large dollar savings in another area."

At McKesson, Polastri agrees that the industry has made tremendous strides in generating savings through

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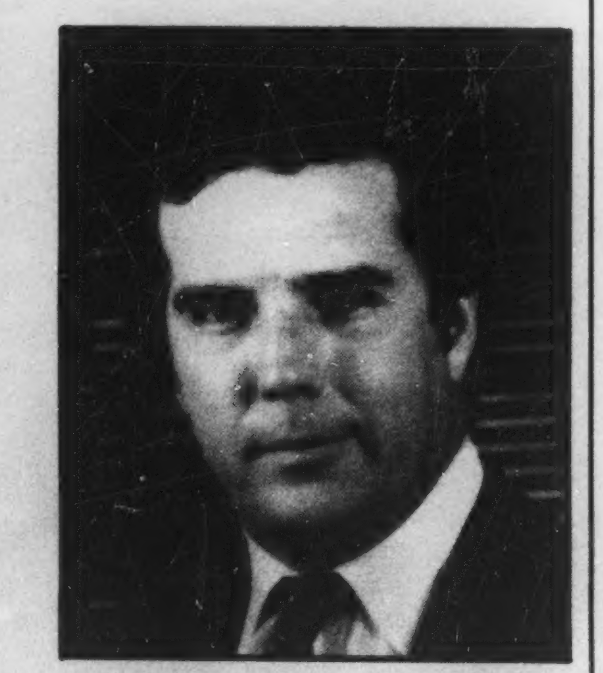

'Once you have four or five guys controlling 90% of the industry sales, you have less to gain from battles for market share increments,

—Bill Tauscher
chairman, FoxMeyer

Wholesaler distribution centers

Company	Number '85-'86	Number '86-'87	Sales per DC (in millions)
McKesson	56	54	$ 73.2
Bergen	43	48	50.0
Amfac	39	37	14.5
Alco	20	26	50.0
FoxMeyer	12	13	100.0
Harris	9	9	100.0
Bindley Western	6	6	105.0
Durr Fillauer	5	5	55.0
Owens & Minor	4	4	109.0
Humiston-Keeling	4	4	80.0
Ketchum	4	4	76.0
Miami-Luken	4	4	15.0
Dik Drug	2	2	No Est.
Louis Zahn	1	1	190.0
Drug Guild	1	1	150.0
Twin Cities	1	1	150.0
Northwestern (Minn.)	1	1	69.0
Walsh-Lumpkin	1	1	55.0
Kendall	1	1	40.0

Source: *Drug Store News* survey

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Warehouse consolidation boosts efficiency

Continued from page 19

technology enhancements. "We're now in the third generation of trying to improve the distribution network by making improvements internally," he noted.

Although Polastri believes that the industry has "done all we can with improving productivity from people," he does think there may be new systems emerging that can yield even higher productivity.

McKesson, he says, is planning an experiment starting early next year with some new systems developed in Europe. Polastri would not talk about the experiment in depth, but said it did not involve robots and was a "different concept and very complex."

McKesson, which is involved in a number of different areas of distribution, is also testing combination warehouses that can put several different companies under one roof, thus eliminating what Polastri calls "the superfluous internal parts of each operation, like accounting, overlapping management layers, etc."

'The blood is out of the turnip as for what we can still achieve with cost reductions.'
—Bill Tauscher
chairman,
FoxMeyer

The first McKesson combo warehouse opened over a year ago in Honolulu, and the second will open next spring in Memphis.

The Memphis warehouse will have four companies under one roof: the drug wholesaling division, the Valu-Rite voluntary division, the McKesson office supply division and the McKesson veterinary supply division.

"We won't need four distribution managers to run this warehouse," Polastri said, "just one. With four companies under the one roof, they'll all use the same warehouse, the same trucks. Before in Memphis, we would have had to have four trucks following the same route. Now we'll have one."

Polastri said McKesson hasn't yet identified all the dollar savings that are possible with the combination warehouse, but he did say the company will open three more in 1988, all in sites not yet announced.

"We'll be consolidating as we go in," he said. "There was a time when we had over 100 distribution centers; now we have 50, and that trend will continue."

Yost points out that of all the drug wholesalers, McKesson is in the best position to continue to develop efficiencies from operational improvements.

This is partly because McKesson generates nearly twice as much dollar volume from its distribution centers as Bergen, its closest competitor, and about three times more than Fox and Alco, the other two members of the top four.

No one else—except FoxMeyer to a smaller extent with its Ben Franklin division—is doing what McKesson is doing. Says Yost, "They're not just a drug wholesaler, but a national distributor of consumable nondurables. They have the mass merchandise division. They're looking at grocery stores, mass merchandise stores and combination stores, all as new avenues of growth."

It is because of McKesson's special situation, sources say, that it can continue to find more cost reductions through technology. However, for most of the smaller local and

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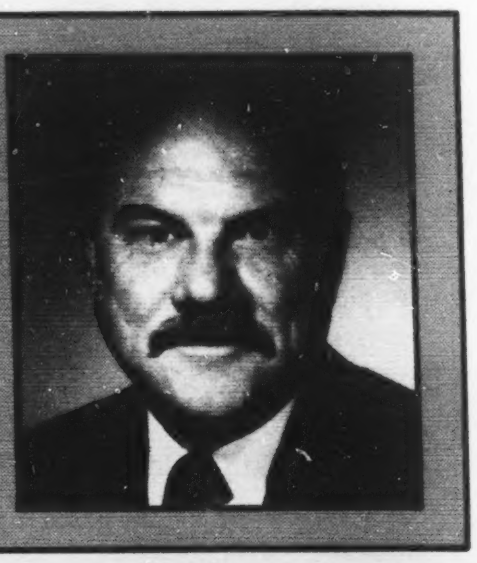
'There was a time when we had over 100 distribution centers; now we have 50, and that trend will continue.'
—Joe Polastri
president,
McKesson Drug



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	Dollar sales: past two years		Sales projections: next two years	
Sales to:	*Increased*	*Decreased*	*Will increase*	*Will decrease*
Independent drug stores	67%	22%	56%	33%
Direct deliveries to chain stores	72	6	61	11
Deliveries to chain warehouses	44	6	39	6
Mass merchandisers	22	0	28	0
Food/grocery/ combination stores	22	0	22	6
Clinics and HMOs	44	0	50	0
Nursing home suppliers	50%	6%	33%	6%
Nursing homes direct	0	0	6	6
Physicians	0	0	0	6
Mail-order houses	17	6	17	0
Hospitals	56	17	61	22
Home health care store owners	33	0	22	6
Retail buying groups	50	6	59	6

Source: *Drug Store News* survey

Continued from page 21

regional companies, that task will be much harder, as it will be for many of the wholesalers in the top 10.

Further reductions difficult

"The blood is out of the turnip," said Tauscher, "as for what we can still achieve with cost reductions. When that's done, the question is will the major wholesalers who are left recognize that we really do have to get a reasonable return on sales?"

Alco Health Services' McNamara also agrees that the industry is reaching "the point where pricing has gone about as far as it can go. Now the wholesaler has to get margins in line to where they're reasonable."

McNamara thinks the industry is approaching the point where competition among the leading wholesalers will no longer be over prices, but over services.

"With the possible exception of buying groups," he said, "no one is concentrating today just on price. People stand or fall on the services they can provide."

McNamara also says that buying groups are hurting the industry's profitability because they sometimes force the wholesalers who bid for their business to pick up products and lines that cannot be efficiently carried in a warehouse.

> *The industry is reaching 'the point where pricing has gone about as far as it can go. Now the wholesaler has to get margins in line to where they're reasonable.'*
>
> **—John McNamara**
> exec vp,
> Alco Health Services

"Some of these products take up lots of cube," he said. "They're slow moving, poor turning. Sometimes they duplicate similar products or lines that we're already carrying, but because the buying groups are interested only in price, they're forcing the wholesaler to carry products that make them less efficient."

Status of price differentials

On the question of manufacturer price differentials, which are generally blamed for much of the problem of illegal diversion, wholesalers say they are still not certain where this practice is trending.

Some say the process is just as widespread as ever and that manufacturers are not doing enough to remove the "inequities of the marketplace." Others are encouraged by the recent actions of manufacturers like Merrell Dow to reduce or eliminate differentials in their system.

Continued on page 24

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'86 ANNUAL WHOLESALER REPORT

Buying groups reduce margins

Drug wholesalers: Voluntary, co-op and franchise services

Company	Voluntary, co-op or franchise	Number of members
McKesson	Valu-Rite	3,000
Bergen Brunswig	Good Neighbor	475
FoxMeyer	Health Mart	500
Alco	Family Independent Pharmacies	1,000
Amfac	ABC Pharmacies	1,140
Harris	Super Service	320
Durr Fillauer	Price Guard	320
Ketchum	PIP	280
Humiston-Keeling	Service Pharmacy	600
Dik Drug	Centsible Drug	135
Louis Zahn	Family Drug Centers	50

Source: *Drug Store News* survey

Continued from page 22

(A differential is the difference between what a manufacturer charges one class of customer, such as a hospital, and what it charges another class—the retail trade through a wholesaler—for the same products. The differentials have often been huge. To make extra money, some hospitals have been known to buy more than they need and then sell the excess product to a wholesaler or retailer at a cost less than what they would normally have to pay the manufacturer for that same product.)

Status of buying groups

Starting in late 1984, many retailers, particularly independents, began to fight back against what they called the "unfairness" of the differential systems by forming buying groups of their own. The groups negotiated directly with the manufacturers for the lowest prices, usually for products carrying the highest differentials.

> *'In the next one or two years, the growth of buying groups will start to level off.'*
> **—Joe Polastri**
> president, McKesson

To get the distribution business, wholesalers were forced to bid for the groups' business. Many wholesalers said the bidding has been "intensely competitive," and that is "one of the chief reasons why margins are eroding."

At FoxMeyer, Tauscher says wholesalers are partly to blame for the rise of the groups. He says that in some instances, particularly with generic drugs, wholesalers have not done a good job "at negotiating the lowest possible acquisition costs," consequently creating a reason for the buying groups' existence.

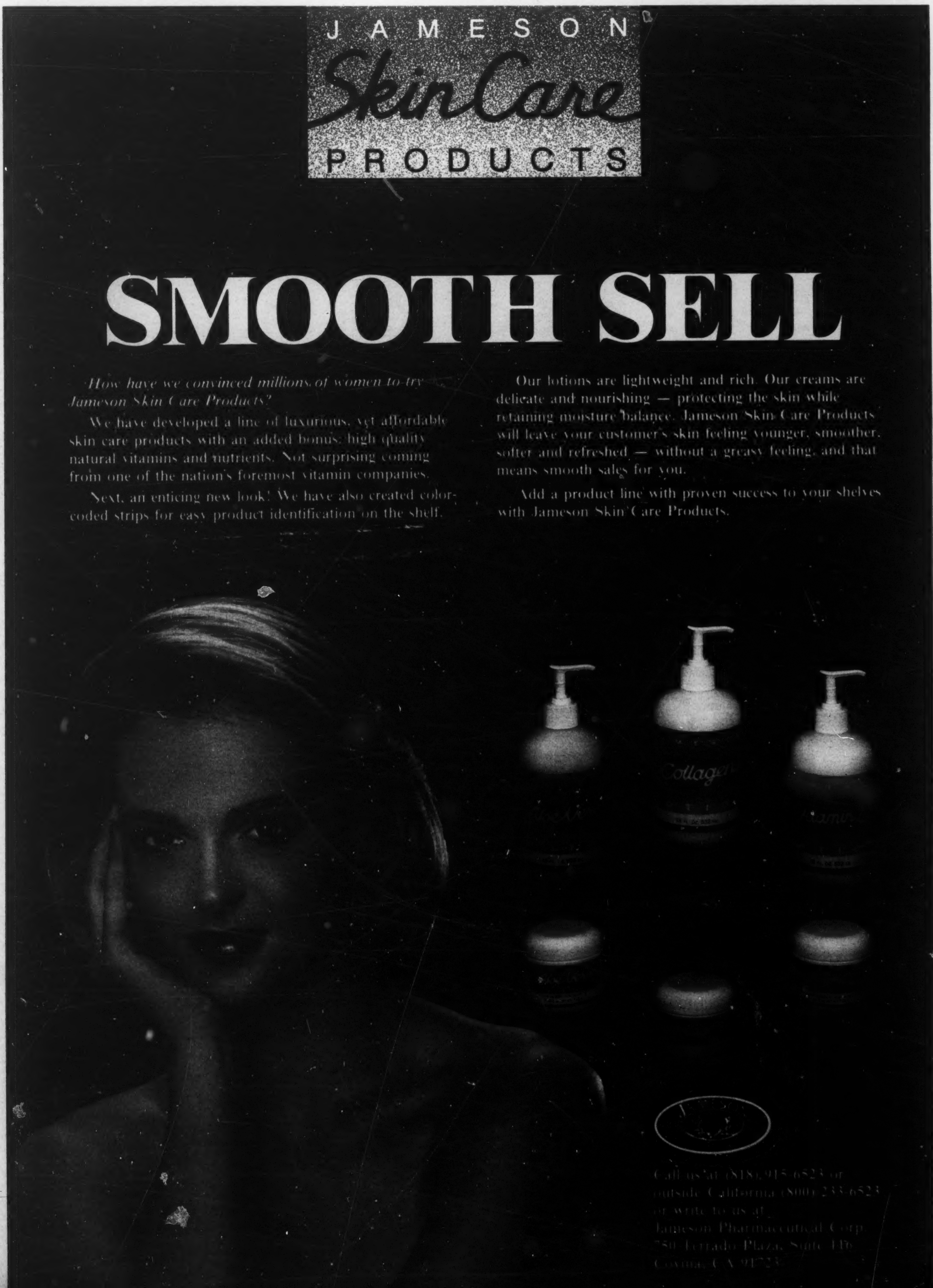
However, he believes wholesalers are now awake to this problem and that they are becoming more aggressive in negotiating better prices.

Tauscher, like most wholesalers, also thinks that the buying groups "exist solely for the purpose of providing price. They cannot offer the services that a wholesaler can offer, and as we as wholesalers start to match them with prices, they will either go away or change into some other form. But I don't think they will continue to operate as we know them today."

At McKesson Drug, Polastri and senior-marketing Fred Toney made a similar prediction. "In the next one to two years, the growth of buying groups will start to level off," they feel.

However, even if buying groups do fade from the scene, there may be a new complication emerging that could be either a threat or an opportunity for wholesalers.

Continued on page 26



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Hospitals remain growth area for industry

Continued from page 24

At Bindley Western, Bill Bindley called the emergence of the practice of manufacturers making prepackaged pharmaceuticals available to physicians a "double-edged sword for wholesalers."

"It could be a source of new users or new business for wholesalers," he said, "or it could eliminate business from our normal source of trade: the retailers."

Bindley said he couldn't tell at this point what the new development might mean for wholesalers, but that the industry will have to take a "wait-and-see attitude."

Clarification of role

Diversion is also a question mark. The Justice Department recently issued an opinion clarifying its position on the legality of secondary source buying, and for the first time there is a formal governmental document stating that secondary source buying is not illegal per se.

Several wholesalers say that last year, after the F.B.I. cracked open a multistate diversion operation involving a number of wholesalers, pharmacists, physicians and manufacturer reps, they were told by Justice officials that all secondary source buying was illegal.

The latest opinion, say wholesalers, is a "180-degree turn from last year's position," and it makes it possible for wholesalers to buy pharmaceuticals from sources other than manufacturers without assuming any overwhelming legal liabilities.

The document states that secondary buying is not illegal per se but that the purchaser, usually the wholesaler, does have an obligation to obtain from the seller authorization proving that the goods being sold are not counterfeit and have been legally acquired by the seller.

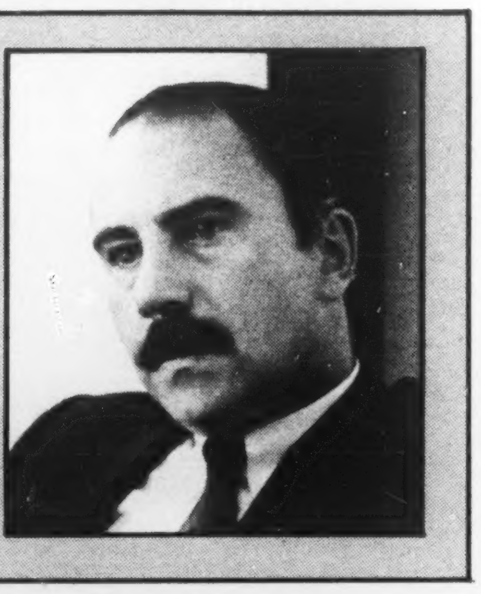
Most wholesalers applaud this latest development, and many of those who have stopped buying from any secondary source for fear of being outside the law said they will now reconsider their options.

"What the new Justice Department ruling does now," explains Tauscher, "is in effect warn the buyer that he or she has a legal responsibility to be sure the purchase is legitimate, especially when they are offered the product at a price considerably below the current market."

Hospital growth

For the past two years, wholesalers have been trying to generate more sales and more profits from diversifying into new areas of business, and in this area, hospitals have been a major source of growth for wholesalers large enough to service this market efficiently.

> *'Independents know that they can only go so far with price, and then they have to attract customers with other services and other strategies.'*
>
> **—Bob Aitchison**
> vp-marketing, health services
> Alco



Last year, wholesalers like McKesson, Amfac and Alco reported dramatic increases in sales to hospitals. This year, however, most of the large wholesalers report that their growth is still good, but the percentage is not as dramatic because of the bigger base.

At McKesson, Polastri said the growth in hospital business in 1986 is so far about 15% over last year. At this time last year, McKesson was recording growth increases of about 30% in hospital sales.

McKesson also said wholesalers have reached the point where they will not lower margins any further in order to penetrate this market.

"The expansion into hospitals will continue," said Polastri, "but not at the expense of lower gross margins.

Other wholesalers said it is "virtually impossible for margins to go much lower in the hospital business. If they did, no one would be making any money."

Besides lower margins, wholesalers also complain about the slowness of the charge-back system in their transactions with hospitals. Most are hoping that in 1986 or early 1987, they will be able to work out with manufacturers a quicker way to be refunded for their investment in supplies for hospitals.

As it stands now, wholesalers have to wait anywhere from 30 to 90 days and sometimes as long as 120 days to get compensated for pharmaceuticals they sell to hospitals, they say. (Charge-backs are the amounts of money manufacturers will refund wholesalers for certain pharmaceuticals distributed to hospitals. Many manufacturers contract to sell certain pharmaceuticals to hospitals at a lower cost than they charge retailers. Wholesalers who distribute these pharmaceuticals to hospitals, based upon the terms of the contracted price, are entitled to reimbursements generally referred to as charge-backs.)

Growth areas

For the smaller or regional wholesalers, most industry sources feel that further sales growth can only come from building onto their existing base of retail customers or through providing more services and a more varied product mix to the customer base they currently serve.

One source said that for the smaller and regional guys, the only market left to develop is the independents.

The top 10 companies, however, continue to look to other trade areas such as hospitals, HMOs, nursing homes, chain drug stores, mass merchandise stores, combination stores and food stores for growth.

However, even in pursuing these markets, size is critical. Several wholesalers said that full penetration of the hospital market is only possible for the top four who can operate simultaneously in a wide variety of geographic markets while providing expanded customized marketing services.

Product mix

The top 10 are also doing the most to expand the mix of products they carry. McKesson is expanding into veterinary supplies, office supplies, hospital and surgical supplies and health care. FoxMeyer is expanding into generics, which Tauscher calls a very attractive market, still undeveloped for wholesalers.

"About 10% of all pharmaceutical sales today," he said, "are done by generic companies, and I'd estimate that wholesalers right now only have about 50% of that business. The rest is going direct or through other suppliers."

At FoxMeyer, Tauscher said generics is "our fastest growing product segment, doubling each month over the prior year."

Home health care is still considered by many wholesalers a very attractive area whose potential is still to be realized. Wholesalers say this market probably will not explode overnight because it is a

Continued on page 28

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'86 ANNUAL WHOLESALER REPORT

Wholesalers target voluntaries

Continued from page 26

"complex business that must be studied and grown in a steady, careful fashion."

As wholesalers consolidate and get bigger, they are trying to pass along some of their savings from efficiencies to customers. For the independent retailers, that has meant a dramatic growth in the past few years in wholesaler voluntaries or cooperatives.

At McKesson, which has the industry's oldest voluntary in Valu-Rite, there are now 2,300 stores in the program, and it is growing at what senior vp Fred Toney calls a dynamic rate.

"We're adding about 100 new stores a month," Toney said, "and the growth is there because we're providing the services that today's independents need."

FoxMeyer's Tauscher says the growth rate in the FoxMeyer voluntary, Health Mart, is just as dramatic. "No one can compete today just on the basis of price," he said. "The retailers need strong servicing to grow as well as survive, and we can see that those who belong to voluntaries and who participate actively in them, as Health Mart members do, do much better on average than retailers who are not members."

At Alco, Bob Aitchison, vp-marketing for health services, said the voluntary Family Independent Pharmacies have now topped 1,000 stores, and the driving force behind their growth is value-added services.

"Independents know that they can only go so far with price," Aitchison said, "and then they have to attract customers with other services and other strategies.

"That's why buying groups are not the answer for the independents. For them to go out past price and try to re-invent the wheel is redundant."

Electronic data transfers

At the National Wholesale Druggists' Association, president Charles Trefrey believes the industry will be able to achieve further cost savings from the implementation of more complex electronic data exchange systems, particularly between wholesaler and retailer.

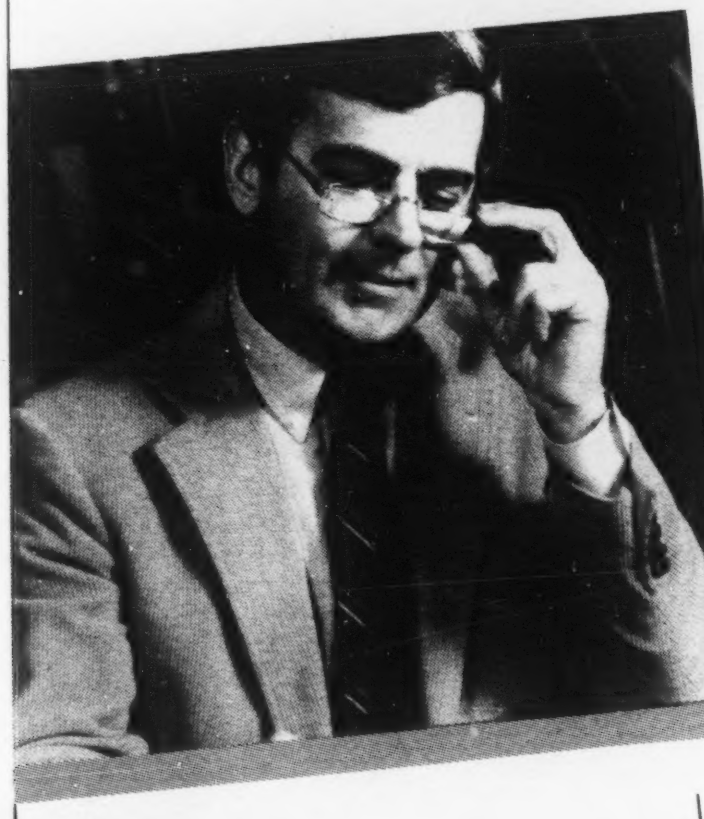
"The majority of companies now have the ability to exchange information electronically," said Trefrey. "What we're doing now at NWDA is help the industry move toward a standardized form of exchange."

Trefrey pointed out that the closing of the electronic link between wholesalers and manufacturers would result in savings similar to those achieved by retailers and wholesalers when electronic order entry systems were implemented: reduction of paperwork, elimination of errors and the expediting of orders.

Bergen's Fay points out that when electronic links are formalized between wholesalers and manufacturers, it might result in wholesalers adding another 20 share points to the amount of pharmaceutical business now done through wholesalers.

In 1985, the Pharmaceutical Manufacturers Association estimates, about 64% of all ethical pharmaceutical manufacturer sales for human use was distributed through drug wholesalers.

If that share were to rise to 85% over the next few years, it would dramatically help wholesalers improve profitability, Fay points out.



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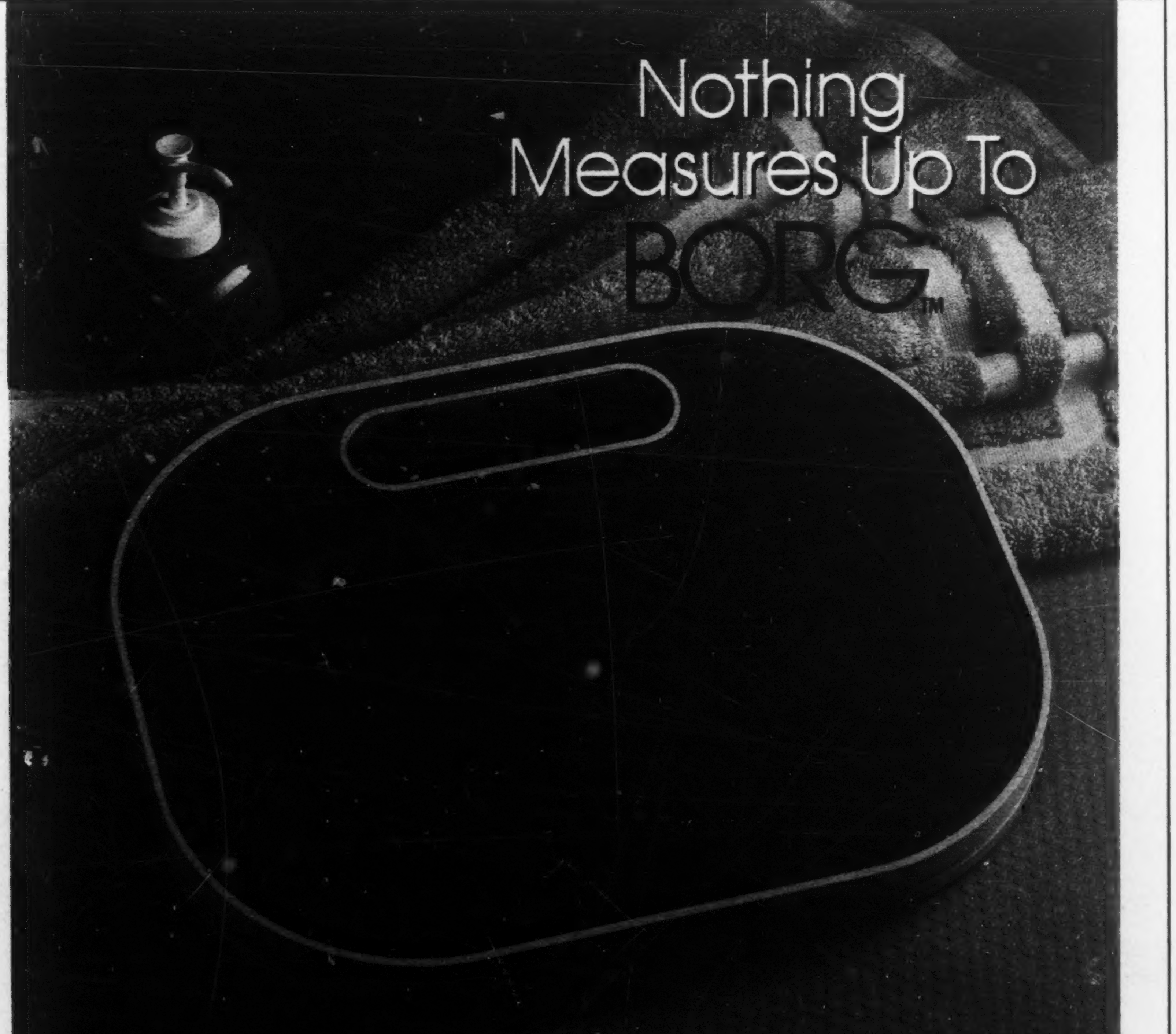

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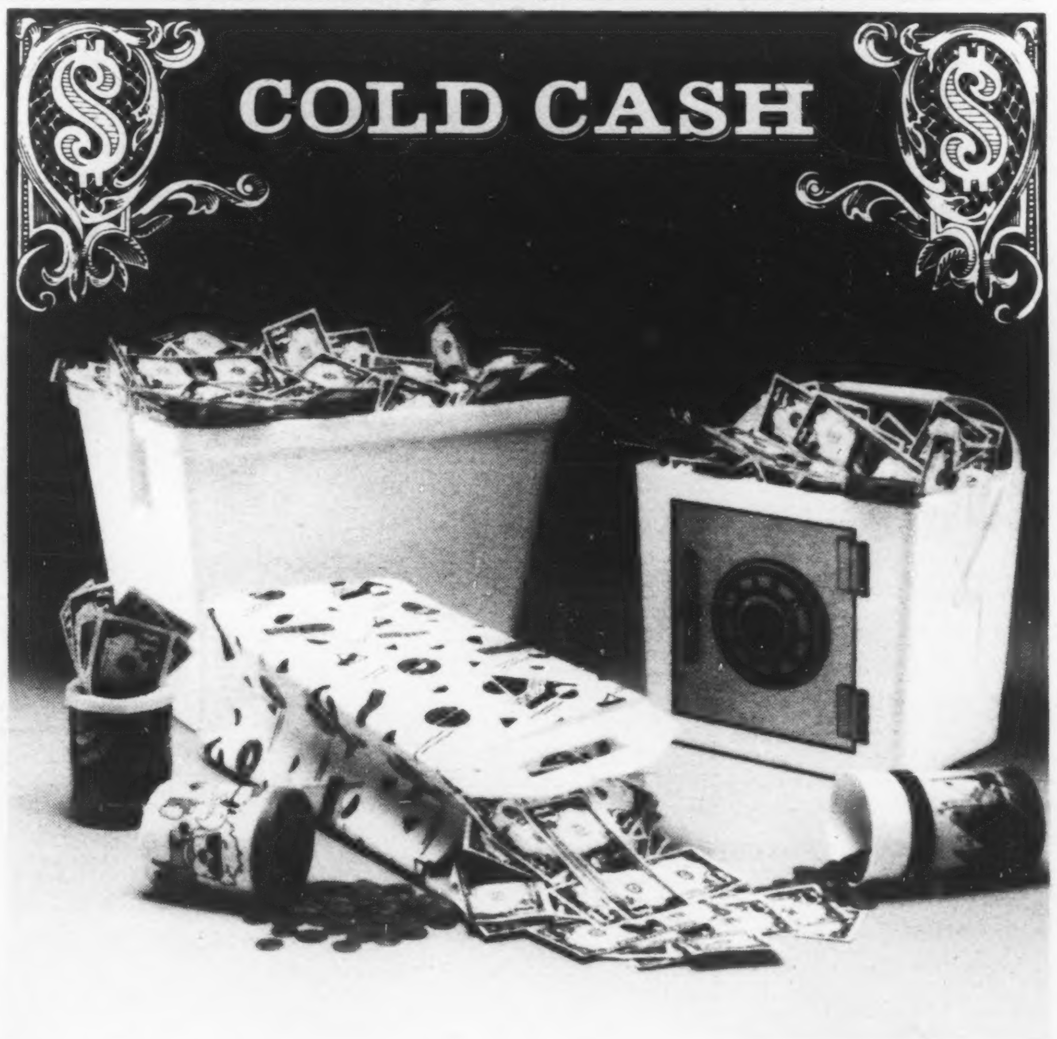

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MERCHANDISING TRENDS

Drug store '85 housewares share climbs to 7%

Surpass supermarkets as preferred retail outlet

CHICAGO — Drug stores are grabbing a larger share of the nation's housewares volume, estimated at $23.2 billion in 1985.

Merchants in the retail drug trade upped their status to become the fourth most popular type of store for housewares merchandise. They snatched a 7% share for the first time in the 20 years the housewares industry has been measured.

The drug store share rose from 5% in 1984 to 7% in 1985, surpassing supermarkets for the first time. The food store share of housewares sales skidded from 7% to 5% in the last full year, according to statistics in the 19th annual study of housewares manufacturers by the National Housewares Manufacturers Association. Some 610 companies responded.

The improved stance of drug stores leaves them behind discounters such as K mart, Wal-Mart and Bradlees; catalog showrooms such as Best Products and Service Merchandise; and department stores.

They're all vying for leading shares of a business that shrank in 1985 for the first time in 16 years. Housewares manufacturers' total dollar sales volume decreased by 5.6% from $24.6 billion a year earlier.

Factors cited

What's going on here? Manufacturers cite "changes in the competitive mix," presumably more low-ticket items in the marketplace, and "increasing impact" of imports.

Retailers would add another dimension to that explanation. Affiliated buyer Donald Vanecek summed up this point of view neatly when he noted "the lack of new merchandise in any category."

Indeed, that's an age-old criticism by retailers, but a probe of the industry would lend support to that statement. Nearly half, or 46% of housewares manufacturers, reported annual sales of less than $2.5 million, leaving little for research and development efforts. Some 24% of housewares manufacturers have an even more acute problem because their sales are less than $1 million.

New products may be the lifeblood of the housewares industry, but manufacturers and retailers differ on whether the blood is flowing.

Skeptical housewares merchants point to the copycat tactics of vendors, who offered so far in the 1980's a half-dozen versions of the downsized food processor originated by the Sunbeam Oskar, and a similar number of imitators of Black & Decker hand-held vacuums and rechargeable lights, as examples.

They contend further that cordless kitchen electrics, under-cabinet appliances and even electronic irons were just modifications of existing products that provided new features, not new function.

Price obsession blamed

On the other hand, vendors blame retailers' price obsession for weak industrywide R&D efforts; they say that caused them to channel engineering efforts toward cost cuts instead of new product design.

A valid question lingers above the debate: How many ways can you open a can, perk coffee, dice food or dry hair? Are there new useful housewares functions left?

It seems for the moment that drug stores will find their best opportunities in microwave cookware and food storage sku's that grew out of increased national household penetration of microwave ovens and a greater stress on convenience by today's consumers. Ultrasonic humidifiers at a magic $39.99 price point are popular because of health concerns, as are electronic blood pressure kits and thermometers to tap shoppers who won't skimp on health-related merchandise.

Welcome to Dart
SEASONAL
Tide
AJAX
RITZ
DART DRUG

Household cleaning and chemicals is becoming a more important traffic-building category in drug stores, as at Dart, Falls Church, Va., which promotes large size laundry detergents by the walk-in.

Drug stores' edge

Drug stores have an edge in merchandising the likes of massagers, humidifiers, blood pressure kits and thermometers because consumers associate drug stores with health. Moreover, the dominant discounter competitors haven't decided where best to display them, so they aren't easily found. Also, pharmacists can explain how to use the items.

Moreover, improved health care technology has led to lower prices and easier-to-use product designs, which has broadened the market. There are also Medicare and Medicaid fund cuts, an escalation of professional health care costs, an aging populace and a willingness among consumers to buy higher-end feature-laden models.

On the other hand, drug store retailers seem to be cutting back on the number of suppliers and sku's they deal with in personal care, often going with one key source and one price alternate, trade sources told *Drug Store News*.

That's making it tough for newer butane-powered hair care appliances to gain shelf space despite their innovativeness.

Retailers said low margins are the problem in personal care, and the shift is part of an inventory management process. That's exactly the problem that colored hair blowers attacked last year by targeting a teen market willing to pay full 30%-35% margins for fashion colors. That worked for a while before retailers started to mark down these popular items as well.

Persistent low pricing in personal care has apparently led to the sku cutbacks, lending credence to manufacturer comments about suicidal price tendencies among retailers.

Rise appears surprising

The increased housewares share at drug stores seems surprising, given the trade's penchant for reverting to core categories in tough times. Indeed, Fay's has cut housewares footage, inventory and ad activity this year, and many chains remain conservative in their approach to the category.

However, several reasons help explain why drug stores are faring better in housewares. Discounters slipped from a 38% share to a 32% share in 1985, leaving a void picked up mostly by catalog showrooms and drug stores.

Drug store merchants have become keener in cherrypicking promotional goods such as humidifiers, low-ticket subcompact microwave ovens and cookware and low-ticket downsized food processors.

In addition, drug store operators have become more adept at using household chemicals, cleaning supplies and paper goods as promotional traffic draws into housewares departments,

Continued on page 87

White is hot!

What colors should drug store merchants consider when ordering housewares items at the November Housewares show? How about white, white and more white.

White was the preferred color in five product classifications, according to manufacturers surveyed by the NHMA. White led in bath accessories, closet accessories, kitchen appliances and accessories, outdoor products and accessories, and serving and buffet products and accessories.

Moreover, white was expected to be even more popular in 1986, respondents said.

They felt white would strengthen its lead in bath over blue to hold a 48% to 26% margin in 1986; in closet over blue, 56% to 14%; kitchen over almond, 58% to 23%; outdoor over red, 37% to 18%; and serving and buffetware over red, 38% to 17%.

Drug stores improve housewares stance

(Mfr. sales in billions of dollars)

	1984 sales	*1984 % share*	*1985 sales*	*1985 % share*
RETAILERS	**$20.4**	**83%**	**$19.9**	**86%**
Discount department stores	9.3	38	7.4	32
Catalog showrooms	2.2	9	2.8	12
Department stores	2.5	10	2.3	10
Housewares/hardware stores	0.7	3	1.4	6
Supermarkets	1.7	7	1.2	5
Variety stores	0.5	2	0.7	3
Mail order	0.5	2	0.5	2
Home centers	0.5	2	0.5	2
*Others**	1.2	5	1.6	7
WHOLESALERS	**$ 4.2**	**17%**	**$ 3.2**	**14%**

*Includes buying syndicates, warehouse clubs, others.
Source: NHMA, B. Angell & Associates

Home health care comes naturally to drug chains

By Dave Vaczek

Drug chains are cautiously advancing into home health care, relying on their retailing expertise and strength as health care educators.

While drug chains are well-positioned as merchandisers and pharmacy professionals, industry analysts say the market has become more complex and uncertain, influenced by the revolutionary trends rocking the health care industry.

Chain officials and wholesalers with programs that supply independents agree the prospect is bright. Although estimates on market size and growth vary dramatically, it is clear that home health care growth will outstrip growth of the general health care market, as economic and demographic trends come to bear, according to industry analysts.

Growth spurred

The aging population and the pressure to control health costs—with the Federal government leading the way—are the two key factors that will propel home health care growth into the next century, they say.

Chains such as Hook, Peoples and Perry Drug have led the way in developing freestanding stores—"home health care centers" designed to offer one-stop shopping convenience to customers, including hospitals and HMOs. Harco and Begley are leaders among the smaller chains, with strings of freestanding units catering to most home care needs. Walgreens has emphasized growth in its Chicago-based home medical centers, and Thrift recently launched a program that supplies durable medical equipment in the Atlanta area.

Independents are expanding their exposure with wholesalers' programs that often provide service support in areas such as claims processing and market positioning.

Natural extension

Chains say they are motivated by more than profit from home care equipment sales. They see home care as a natural extension of their professional services, since the two often serve the same geriatric or ailing customers. The new departments also reinforce the health care image.

New competitors are coming into the market from all sides. But today's highly fragmented market is already undergoing a shakeout, marked by consolidation and dropouts.

"Consolidation is inevitable. The market is highly fragmented, with 5,000 to 6,000 companies supplying services and an equal number providing equipment," said Teri Louden, president of Louden and Company, a Chicago-based health care consulting and information service firm.

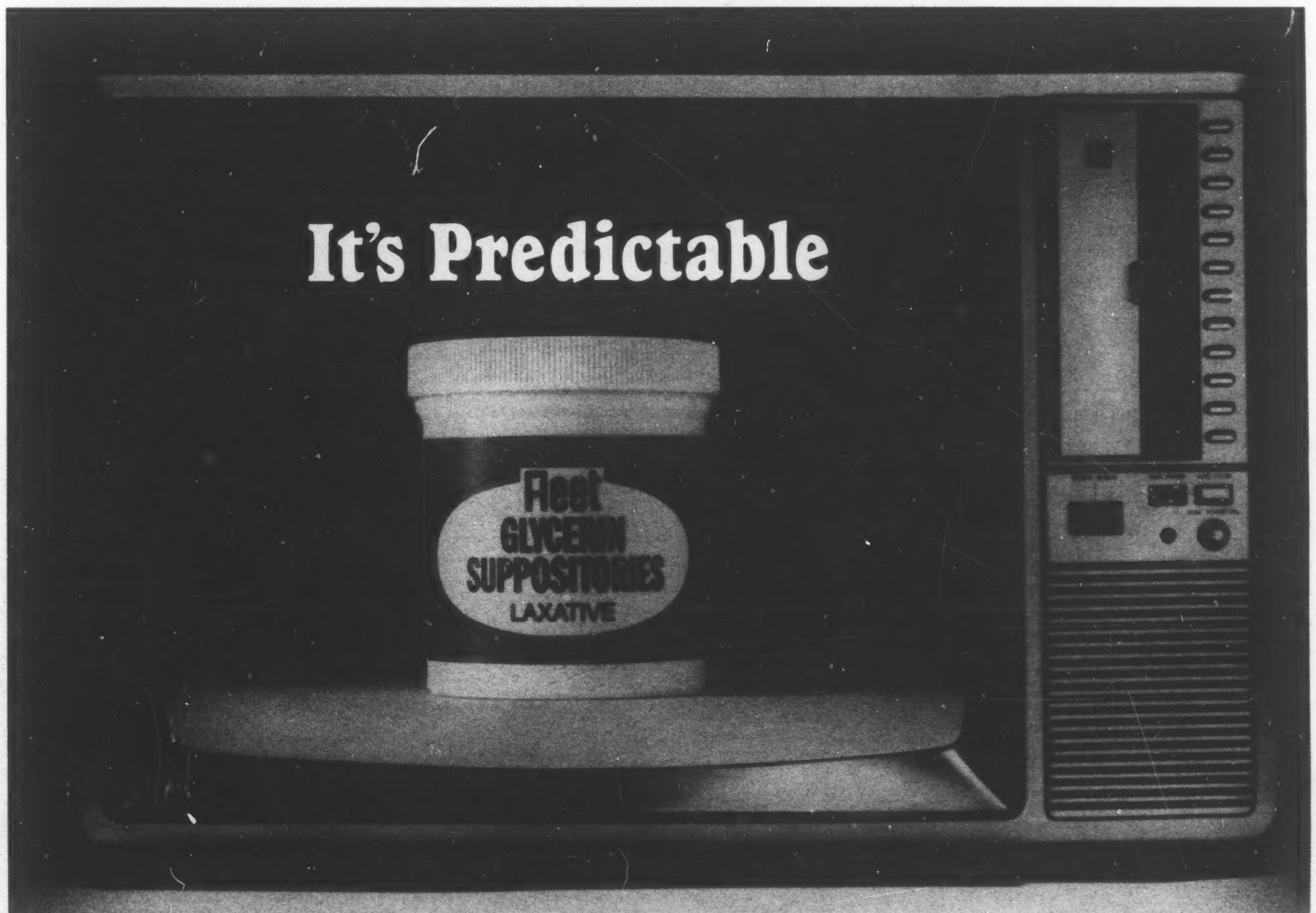
HOME HEALTH CARE

Hospitals and HMOs are rushing into home care as competitors to drug stores and as customers. Traditional suppliers of home care products, such as DME dealers and home health care agencies, are expanding their businesses or merging.

The uncertainty in the market is also being fueled by the Federal government's drive to contain health care costs, which will lead to further controls on home care reimburse-

Continued on page 56

Perry Drug Stores staffs Comfort Care Center in Pontiac, Mich., with full-time home health technician. Here, staffer Linda Brooks assists a customer.



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3. Three high-profit deals a year.
4. Co-op advertising allowance.

Stock and promote the one brand that is aggressively advertised and promoted, the brand that is making sales and profits for you.

fleet pharmaceuticals

Circle #014 on Reader Service Card

Chains eye cost-curb impact

Continued from page 55

ment and possibly to a capitation system similar to the prospective payment system imposed on hospital costs in 1983.

Rules limiting cost continue to be adopted by the Health Care Financing Administration. Last month, H.C.F.A. endorsed a rule that would give the agency the same right now enjoyed by Medicare carriers to impose limits based on what is determined "inherently reasonable."

On the table is a plan to extend "lowest charge levels" that control reimbursement levels (and have until now applied to wheelchairs and hospital beds) to about 80 additional DME items. The new guidelines follow a 1985 rent/purchase guideline that requires Medicare recipients to purchase DME items priced at under $125, and purchase rather than rent higher ticket items in cases where a sale is more cost-effective.

The new laws compound the task of Medicare billing. Chains say the impact on sales is less than clear at this time, but will likely drive down prices.

HMOs and PPOs

HMOs, PPOs and private insurers are hot on the government's trail in their own efforts to curtail health care costs. HMOs and PPOs are price shopping for services and are increasingly using utilization reviews that screen providers' performance, said Louden.

"HMOs and PPOs are dedicated to reducing health care costs, and like others before them, they will look to home health care to aid in this process," Louden observed.

The forces of competition and cost containment have already been felt in areas such as DME, where pretax profit margins have shrunk from the 25%-30% levels of two years ago to 12%-15% today, according to Michael Hamilton, president of Diversified Medical Management, a Birmingham, Ala., consulting firm.

Profitability cut

"The average profitability in the DME industry has been cut roughly in half in the past two years," said Hamilton, citing forces including increased expenses and pressure on prices from competition and Medicare.

One home health care official of a large drug chain said that DME remains attractive in spite of these leveling forces allowing a profit of $75 on a wheelchair, compared with $150 several years ago.

"We are receiving outrageous margins. They're becoming more and more realistic," he said.

Drug stores are favorably situated in two respects against the emerging competition, analysts say.

Their pharmacy services—where pharmacists are perceived by the customer as trusted educators—give them an edge against such competitors as DME dealers and other health equipment companies, who are accustomed to selling products through hospitals, with little customer contact.

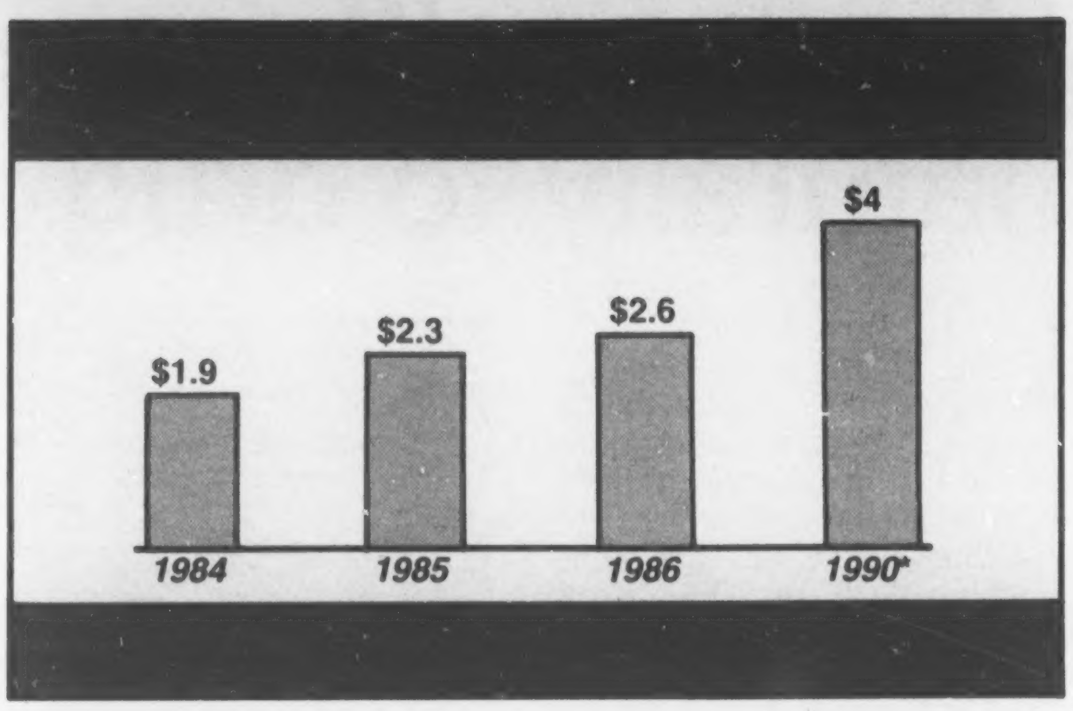
Chains also have a leg up on hospitals and HMOs with their expertise in merchandising.

But these strengths don't guarantee success in a market that is highly segmented.

For each category, different reimbursement rules will apply, the customer base will vary and competition and pricing will vary depending on the market.

Said Louden: "You need to segment the market very

Continued on page 57



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Cold Sore Lip Balm. "It Works!"

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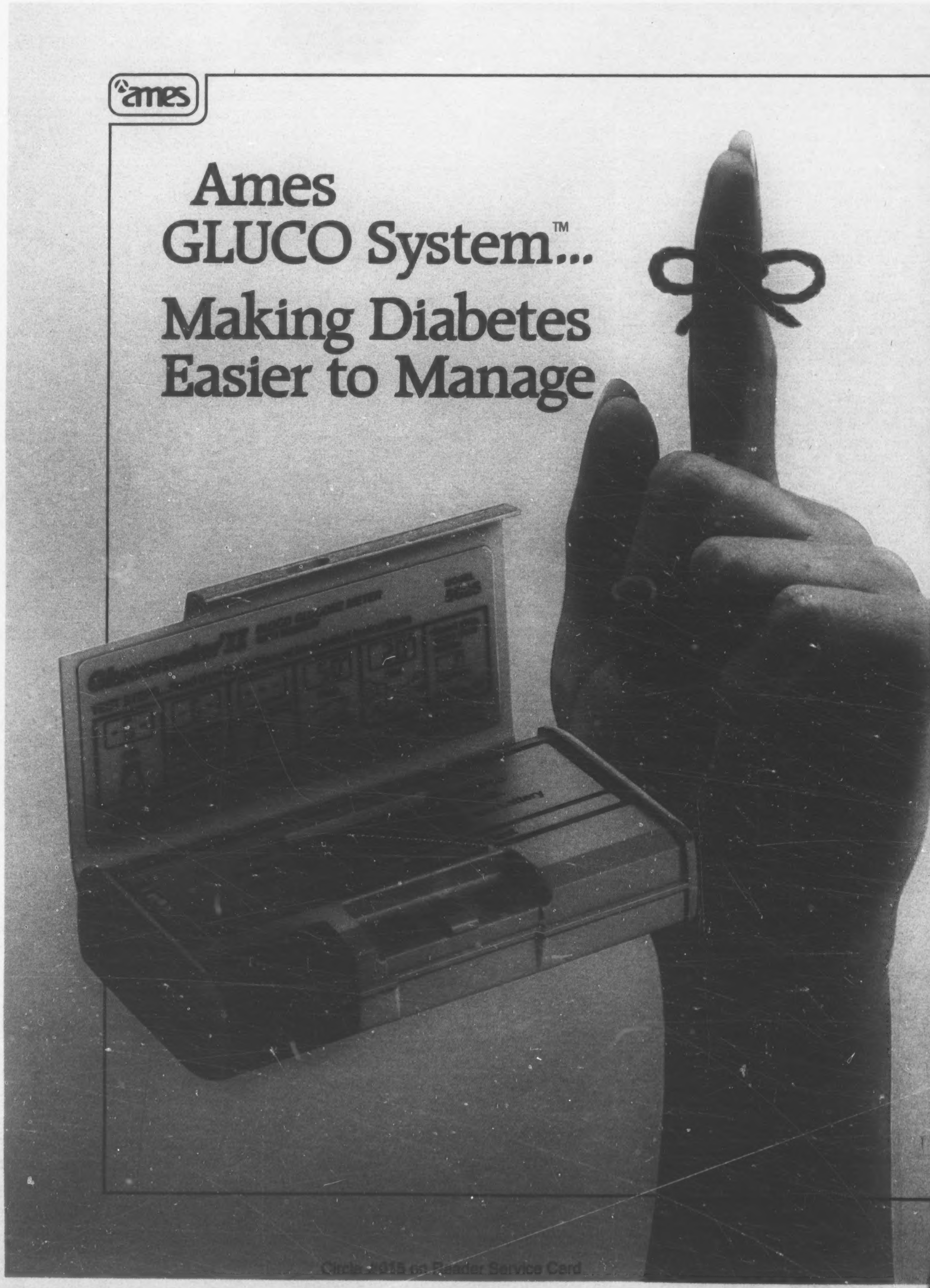
Circle #033



Trained technicians who are sensitive to customer needs play an integral role in Peoples' health care operations.

Wholesalers steering indys to home health care niches

Continued from page 56

carefully. There is an opportunity in selected segments, but every one of the segments is different and has to be appraised differently."

Responding to this fact, wholesalers are guiding independents into niche markets, based on the local opportunity and the services they can afford to offer and feel comfortable in providing.

Chains with complete home health care centers must emphasize reaching the large majority of customers who purchase through referrals from health care professionals, and retaining customers through professional service, observers say.

Peoples Drug has emphasized detailing to doctors, hospital discharge personnel and others who influence where customers buy products in building its program around four stores, two in the Washington, D.C., market and one each in Virginia Beach and Richmond, Va.

Emphasis is also placed on staffing stores with people who are sensitive to customers' needs and who complete the chain's training programs to be health care technicians.

Recognizing that customers are becoming more product aware and more independent from institutional advice, Peoples also emphasizes direct-to-consumer advertising with weekly newspaper ads and a product catalog displayed in all its stores.

Wellby Drugs, on the other hand, has set its home health care program on a new track to sharpen Medicare billing and detailing, according to Richard Legere, pharmacy specialist at the Portland, Me.-based chain.

"We really weren't talking to the people who did the referrals," Legere admits. Medicare billing became snagged as a result of lack of expertise.

Wellby's Med-Supply program is based on a contract with National Medical Home Care, which supplies products to customers after they place the order in a Wellby store. To attract patients, the stores displayed fliers describing the service and offer an 800-WATTS number.

"This was very confusing, since our pharmacists had no real contact with the patient," said Legere.

Rxer turns billing specialist

The chain has since designated a former pharmacist and systems coordinator as Medicare billing specialist. Customers now order products through the store pharmacist, and products are delivered through the stores, to promote pharmacist-customer contact and build the health care image, Legere noted.

The chain is experimenting with 1,000-sq.-ft. in-line departments in two stores in Brewer and Skowhegan, Me. The chain is also redirecting efforts to boost its detailing program. Pharmacists have become more interested in the program with NMHC, now that they have a more central role.

"We're not trying to get in to dominate, but to offer an additional professional service to our customers. But if in six months we don't see an increase in referrals, we would really have to question our involvement in this program at all," Legere said.

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Ames Division MILES

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Circle #033

Study finds OTC buyers want more detailing

Representatives of over-the-counter drug companies are not making the most of their detailing visits with chain and independent OTC buyers.

According to *Drug Store News'* 1986 OTC Buyer Feedback Survey, buyers at the 30 chains and independents polled are generally satisfied with the frequency of visits, but are less than satisfied with the information they receive on topics they feel are important.

Buyers rate services

The buyers were asked to rate 15 areas of service they considered important and to indicate their degree of satisfaction in each area.

While the survey found that there was improvement in 13 of the 15 service areas over last year (when this study was last conducted), most of the buyers still were not "very satisfied" with those services they felt of prime importance.

Chain satisfaction low

For instance, 80% of the chain buyers said they considered the company's return goods policy and co-op advertising highly important (with the latter being considered most important). But less than half (44%) of those 80% were very satisfied with the information being offered by the reps on return goods policy, and only one-third (33%) were satisfied with the co-op advertising information being provided.

Other areas where reps appear to be missing the boat include:

- Display allowances (while they were considered important by 70% of the buyers, only 24% were very satisfied with information being received).
- Upcoming consumer ad campaigns and promotions (considered important by 77%; only 35% satisfied).
- Invoice dating (considered important by 77%, only a 30% level of satisfaction).
- New product information (considered important by 77%; 43% satisfied).
- Case allowances (67% considered important; only 25% satisfied).

Low importance-high satisfaction

In contrast, the data showed that some of the highest satisfaction levels are being provided in areas the buyers considered of low importance. For example:

- Product movement (27% considered important, 56% satisfaction level).
- Cents-off consumer coupon programs (27% considered important, 67% satisfaction level).
- National market share (23% considered important, 57% satisfaction level).
- New display materials (20% considered important, 50% satisfaction level).

Regarding planograming, at least there was some consistency. It carries a low priority among chain buyers (10% importance), and not one of those buyers was satisfied with planograming information being offered.

Independents have different needs

Independent OTC buyers narrowed the field of services considered highly important to them to only two: return goods policy (87% said it was important) and new product information (57% said most important).

Visitation frequency OK

Most of the buyers who were surveyed said they were satisfied with frequency of detailing visits.

The majority (94%) said they were visited twice a year or more, and that suited them just fine. Less than half (43%) said that they were visited more than once a month, while 28% said they had monthly visits, and 23% were visited once every two to six months.

The survey *did* reveal, however, that chains are visited more frequently. On average, the chains receive visits once every 1.4 months, compared with once every 2.4 months for the independents.

Overall, both were satisfied with the frequency of visits they were receiving. Only 10% said they would like more visits, and 8% said they wanted to be visited less frequently.

As might be expected, a larger percentage of independents than chains indicated they would like more frequent visits (17% of the independents vs. only 3% at the chains).

OTC mix

OTC buyers from both the chains and independents were asked how they would describe their OTC product mix.

Nearly three-quarters (70%) said they "carry most of the major brands and sizes available to give shoppers a broad variety of selection."

Less than one-quarter (20%) indicated they "carry at least three to five brands in the major OTC categories," and only 10% said they "carry only the No. 1 and No. 2 brands in most OTC categories."

More of the chain buyers (83%) said they "carry most of the major brands and sizes . . . " than did independents (57%). Only 13% of the chains said they "carry at least three to five brands . . . " compared with 27% of the independents. Only 3% of the chains said they only "carry the No. 1 and No. 2 brands . . . " compared with 17% of the independents.

Pricing strategies

Both chain and independent buyers were also asked to choose the pricing strategy that best described them.

No *one* strategy was picked out by a majority, but more than one-third of the buyers (35%), said, "We stay competitive with other drug stores in our market." This was followed by 28% of the buyers responding with, "We have a full-service/full-price orientation." Twenty-three per cent said that "to bring in shoppers, we rely on sales and low promotional prices rather than low everyday prices." And 12% answered, "We rely on everyday low prices with little or no advertised sales." None chose the category "never being undersold."

The chains more often chose the strategy "full service/full price orientation" (37%), while independents most often (40%) chose "we stay competitive."

OTC product advertising

More than three-quarters (80%) of the OTC buyers said they advertise OTC products once a month or more, up two percentage points from last year.

But on closer examination of the data, it was shown that advertising frequency is behind what it was last year.

This year's survey showed that buyers are more likely to advertise once or twice a month (45%), compared with

Continued on page 73

Services rated "very important"

Service	Type of Company	
	Chain	Independent
Merchandiser promotions		
Return goods policy	80%	87%
Display allowances	70	30
Case allowances	67	20
New display materials	20	17
Obtaining information		
New products	77	57
Regional market share	43	23
Consumer consumption/usage patterns	33	13
Product movement	27	13
National market share	23	7
Consumer promotions/advertising		
Upcoming consumer ad campaigns and promotions	77	30
Co-op advertising	80	20
Consumer rebate program	50	33
Cents-off consumer coupon	27	20
Miscellaneous services		
Invoice dating	80	57
Planograming	10	17
Other	23	13

Source: Lebhar-Friedman research

Pricing strategies in OTC dept.

Strategy	Type of Company	
	Chain	Independent
We stay competitive with other drug stores in our market	30%	40%
We have a full service/full price orientation	37	20
To bring shoppers in, we rely on sales and low promotional prices rather than low everyday prices	27	20
We rely on everyday low prices with little or no advertised sales	3	20
We are never undersold	—	—
Don't know/No answer	3	—

Source: Lebhar-Friedman research

Satisfaction with services among independents

Services of high importance	Percent "very satisfied"
Return goods policy—87%*	34%
New product information—57%	23
Services of moderate importance	
Invoice dating—40%	31
Consumer rebates—33%	30
Upcoming consumer ad campaigns/promotions—30%	36
Display allowances—30%	46
Services of low importance	
Regional market share—23%	25
Cents-off consumer coupons—20%	33
Case allowances—20%	33
Co-op advertising—20%	43
New display materials—17%	80
Planograming—17%	20
Information on product movement—13%	25
Consumer consumption/usage patterns—13%	60
National market share—7%	50

Source: Lebhar-Friedman research
*% who reported important

Satisfaction with services among chains

Services of high importance	Percent "very satisfied"
Return goods policy—80%*	44%
Co-op advertising—80%	33
Upcoming consumer ad campaigns/promotions—77%	35
Invoice dating—77%	30
New product information—77%	43
Display allowances—70%	24
Case allowances—67%	25
Services of moderate importance	
Consumer rebate program—50%	33
Regional market share—43%	46
Information on consumer consumption/usage patterns—33%	40
Services of low importance	
Information on product movement—27%	56
Cents-off consumer coupons—27%	67
National market share—23%	57
New display materials—20%	50
Planograming—10%	0

Source: Lebhar-Friedman research
*% who reported important

OTC products featured in print ads climb 10%

Continued from page 71

once or twice a week (35%), whereas in 1985 the reverse was true.

As a group, the chains reported advertising more frequently than the independents. This year's survey also showed that weekly frequency has dropped among independents (from 37% to 20%) while remaining relatively stable among chains (a slight drop from 53% to 50%).

The study also showed that the number of products featured in print ads increased nearly 10% this year. In 1986, OTC products accounted for an average of 54.2% in advertising done by both the chains and independents, compared with 43.2% in 1985.

The survey gave one possible explanation for the increase in the percentage of OTC products in an average ad, and that was a decrease in the total number of products advertised. In 1985, chains ran an average of 84.2 total products in an ad, while in 1986, the average was 68. The same was true for independents. In 1985, the average independent ran 36 products in a typical ad, while in 1986, the average was 25.5

Of the advertising that is done, the majority is print. The survey showed that 54.2% of all OTC advertising is done in the print media, up from last year's 43.2%.

OTC sales increase

Once again this year, OTC sales increased just slightly over 10% (10.9% this year vs. 10.5% last year). Seven per cent of this year's respondents said sales have decreased, compared with 5% in 1985.

The sample was split on the reasons for the sales increase. Twenty-four per cent reported that the increase was due either to pricing elements or better advertising promotions and/or displays.

In that group that claimed pricing was a key factor in the increased sales, 8% said it was because of increased prices, while 12% felt they made it up on volume sold when prices decreased.

Other reasons offered for increased sales were more new/larger stores (reported by 16% of the sample); more sales, inventory or population (14% reported this reason); and new products/more items available on OTC status (cited by 12%).

OTC space allocation

Asked whether the space allocated to OTC products had increased or decreased over the past year, 43% said store space had increased an average 18.4%. Only 5% reported a decrease. Fifty per cent said there had been no change.

The survey revealed that more chains have increased space for OTC than independents. The increases have also been bigger for the chains.

Half of the chains surveyed said space was increased an average of 21.6%, compared to 37% of the independents polled, who said their shelf space increased 14.5%.

More than half (53%) of the independents reported that OTC shelf space had remained the same, and 10% said it actually decreased. None of the chains reported a decrease, while less than half (47%) of the chains reported no change.

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Circle #034

If FDA decontrolled Rx advertising

WASHINGTON — What would the world of U.S. pharmaceutical advertising be like if there were no Food and Drug Administration?

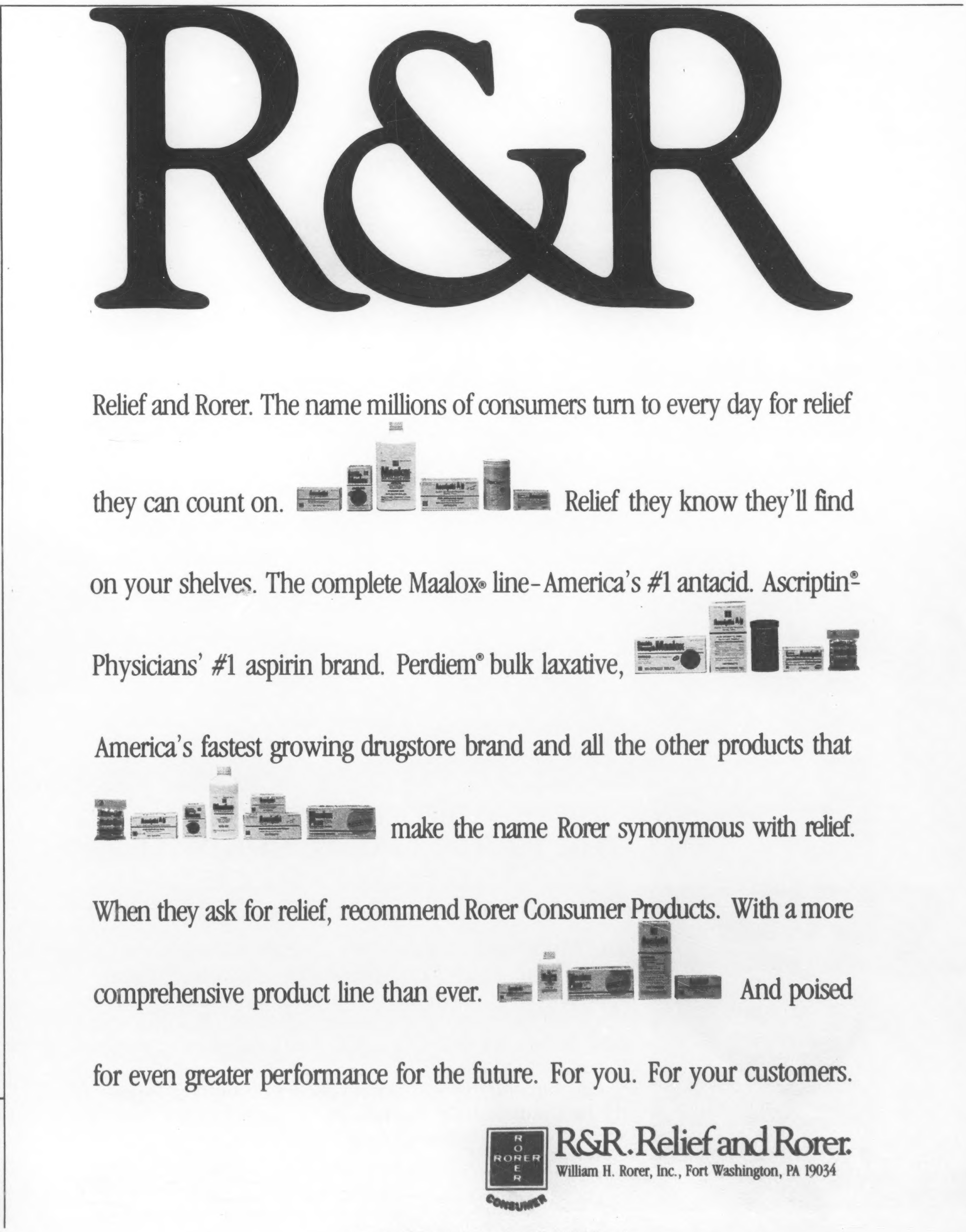
Free marketplace controls would effectively take over for F.D.A. regulations, but at a financial cost to pharmaceutical manufacturers, according to Thomas K. Beckett, marketing communications director at Merck Sharp Dohme, who posed the question at a recent Food and Drug Law Institute seminar.

Claiming that product liability concerns are already more important than the threat of F.D.A. regulatory action, Beckett said design and approval liability would be "the single most influential moderating element" in Rx advertising if there were no government ad controls.

Other potential free market controls would be the "sophistication" and "healthy skepticism" of health care professionals, "the commercial value" of company credibility and integrity, the likelihood that competitors would exploit false claims, and the personal integrity of pharmaceutical marketing personnel.

On the other hand, Beckett warned, eliminating the F.D.A. drug advertising division in favor of free market forces would be financially costly for the pharmaceutical industry. While "mistakes in judgment" would be exposed and corrected by the free market process, pharmaceutical companies could lose customer credibility and business during the process, and might face expensive litigation via consumer product liability suits or Lanham Act proceedings by competitors.

The F.D.A. Division of Drug Advertising is serving pharmaceutical industry interests "whether we like to admit it or not," Beckett said.



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Circle #025 on Reader Service Card

LaVerdiere's moves to fill management board vacancies

John A. McDonald

Donald T. Deschaine

WATERVILLE, Me. — LaVerdiere's Super Drug Stores has made changes in the executive board that reports to president Stephen J. LaVerdiere.

The moves fill vacancies on the senior management board created earlier this year when LaVerdiere assumed the presidency and MIS head Paul Page left the 58-store chain.

Jeffrey R. LaVerdiere was promoted to vp-management information systems, replacing Page, after serving the past two years as assistant vp-MIS.

Samuel S. Dahlquist was promoted to assistant vp-pharmacy operations, regarded as the top pharmacy spot in the company, after serving as head pharmacy supervisor since 1981. He will fill the function left by Stephen LaVerdiere, who was vp-professional services until his own promotion in February.

In addition, John A. McDonald was promoted to senior vp-finance and Donald T. Deschaine to senior vp-store operations.

The board now includes Michael LaVerdiere, executive vp responsible for purchasing, advertising, distribution and the arcade division; McDonald; Deschaine; Jeffrey LaVerdiere; Bruce Carrier, vp and corporate counsel; and Dahlquist.

Pay 'n Save's new ceo walks tightrope

Continued from page 1

man, signaled further adjustments when he said that because the public is asking for better quality—while still eager for bargains—promotional merchandise is being upgraded and price points raised.

Chain of command

In Pay 'n Save's chain of command, Nathanson will have the responsibility for day-to-day operations and Zimmerman will be responsible for overall operations—especially imports, where Zimmerman's longstanding international contacts have resulted in exceptional buys.

Nathanson enters the Pay 'n Save fold with a reputation as a strong leader. His merchandising career is rich.

Much of his career has been with Montgomery Ward affiliates. From 1967 to 1976, he was senior vp-operations, senior vp-merchandising and subsequently president and ceo of Jefferson Stores, which was sold to Montgomery Ward in 1973.

From 1977 to 1978, he was president and ceo of J. M. Fields, the general merchandise subsidiary of Food Fair. After a stint as vice-chairman of United Department Stores, he was named chairman and ceo of Jefferson Ward, a Montgomery Ward subsidiary that closed at the end of 1985. After Jefferson Ward—and continuing into 1986—he was vice-chairman of McCrory Stores.

Experience in departments

Nathanson has had experience in H&BA, OTC and pharmacy because he ran those departments at Jefferson Stores. "They were major departments, and we did a big business," he told *Drug Store News*. "I learned enough so that when I took a look at Pay 'n Save, I could see the tremendous underlying strength of those departments."

The crucial question at Pay 'n Save is: Will Nathanson be able to avoid the fate of Culver, his predecessor? Culver, with many years of drug store experience—and acclaimed in the trade as a "merchandising genius—believed in strong drug departments and felt that too much Zimmerman-type merchandise would erode the drug store's basic function and result in reduced traffic and lower volume.

Zimmerman's philosophy—at least in the beginning—boiled down to: "Who needs a drug store?"

Views clashed

The long and short of it: Zimmerman wanted more space for promo merchandise ("the heart of Pay 'n Save," according to Pay 'n Save ads), while Culver wanted more space for drug departments.

Culver admitted to intimates one other source of irritation: that he was working under extreme tension because he was in the middle of continuing conflict between partners Julius Trump and Zimmerman. The nature of the conflict is not known.

So Nathanson has his work cut out for him. He rates high on the "personality" scale. He has a friendly manner, but he is also resolute in purpose; he gets things done.

He will have to get them done fast, because Pay 'n Save is losing money—$23.6 million in the first nine months of the current fiscal year.

Cleaner's fast turnover pulls traffic

Continued from page 3

where shoppers are prone to impulse buy other than full margin 35%-45% margin housewares products.

Merchandising strategy

Marvin Gresham, president of Gresham Drug in Florida, said he keeps household cleaners in their everyday permanent housewares display area, even when on promotion,in order to draw shoppers to the center of his stores. "We find a big turnover in apartment buildings near our stores. People have an ongoing need to buy and replenish these cleaning items," Gresham said.

That merchandising strategy has been one factor that has helped drug stores step closer to the third ranking, held by department stores with a 10% share of housewares business.

The survey indicated further that retailers are buying housewares direct more and more often, continuing a long-term trend. Manufacturer sales to retailers accounted for 86% of their volume in 1985, with just 14% going to distributors. That compares with an 81%/19% ratio in 1980 and a 60%/40% ratio in 1972. One has to look back to 1969 to find the last time that sales to distributors outpaced sales to retailers, by a 51%/49% ratio.

Excess inventories

The survey, conducted for NHMA by B. Angell & Associates, didn't explain why the dominant discounter share slid by four percentage points. But many discount department store chains were caught with excessive inventories following an unexpectedly weak 1984 Christmas season. They spent the first few months of 1985 working off stocks, often at deep markdowns that helped to spawn a more cautious buying approach through 1985 and 1986.

Drug stores, on the other hand, weren't caught as badly, and were able to buy at more natural levels, balanced to their needs, than discounters since early 1985. Drug store operators recognize their stores aren't the first choice for housewares purchases, so they needn't be as deep or broadly selected in the category as discounters.

Speaking of today's mandate to cut expenses, drug retailers "would rather risk being out of stock than have to take markdowns," Vanecek said.

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Excellent commission. Please submit resume along with cover letter detailing number of sales persons, exact area of coverage, trade classes serviced, top three lines you sell and the type of accounts you are presently selling to:

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*Established company with unique footcare product line seeks **distributors and rack jobbers** to service independent drug stores in southern FL, mid Atlantic and New England markets. Fast turning, high quality, high profits. New introduction in product category. Offers retailers and consumers* "An Alternate Choice."

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And when they go looking for the best people?
It's logical that they put their classified
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people are looking.
Career-minded people shop *Drug Store News Classified*.

The best place to find the best people.
And that's logical.

C5150 -2

REX Awards:
Detailed report on the winners—p. 13

C.E. Lesson:
Calcium channel blockers—p. 33

Merchandising Trends:
Retailers develop private labels—p. 23

DRUG STORE NEWS®

Vol. 8/No. 25 **Serving chains, wholesalers and high-volume independents for 57 years.** Published by Lebhar-Friedman Inc. November 24, 1986

Revco takes LBO finance plan to SEC

By Dave Vaczek

TWINSBURG, Ohio — Revco management has filed a proposed notes and securities offering with the S.E.C. that details planned financing for the $1.25 billion leveraged buyout.

Anac Holding Corp., and Anac Merger Corp., the companies formed by a management-led team to take over Revco, filed the registration statement Nov. 6.

The filing snuffed a rumor that surfaced a week earlier that the financing for the deal was in jeopardy. It led to a slight dip in Revco's stock price, but the stock rebounded and closed at 36⅞ on Nov. 6.

Deadline pressure

Analysts said Revco management is under strong pressure to complete the buyout by Dec. 31, in order to retain advantages of the current tax law, which will be eliminated in 1987. By completing the deal this year, management would be able to retain significant benefits from an expiring tax provision, under which acquiring companies can write up the stated value of assets and thereby boost cash flow from higher depreciation credits. Also, the buyout group and Revco shareholders will incur stiffer capital gains taxes on profits stemming from the sale if it occurs next year.

*See **Revco**, page 7*

Revco management details financing

Note sales:
- $400 million of Anac Merger senior subordinated notes
- $225 million of Anac Merger subordinated notes
- $75 million Anac Merger junior subordinated notes

Stock sales:
- 6,650,000 shares of Anac Holding cumulative exchangeable preferred stock
- 300,000 Anac Holding common shares

Also:
- 300,000 common stock puts of Anac Holding
- Private placement of convertible preferred stock by Anac Holding
- Bank financing

Pay 'n Save's Jenkins out; chain beset by fiscal woes

Ex-president's departure follows Culver exit

SEATTLE — Maynard Jenkins, president and coo of the 140-store Pay 'n Save drug chain, has resigned to become president of Orchard Supply Hardware, a 20-store operation owned by Wickes Cos.

Jenkins' exit from Pay 'n Save follows by several weeks the resignation of Al Culver, vice chairman and ceo. William Zimmerman remains as chairman.

An inside source says that Jenkins, who joined Pay 'n Save a year-and-a-half ago, was frustrated by Pay 'n Save's sagging fortunes. Pay 'n Save has a net loss of $23.6 million on sales of $384.3 million for the nine months ended Aug. 2.

'Offered good opportunity'

Jenkins denies that's why he left. "I was offered a good opportunity in California to run a company," he told *Drug Store News*. "I am a hard goods merchandiser at heart." He had been vp-gmm hard lines at Gemco.

Yet other sources believe that Jenkins' departure is tied to Pay 'n Save vice-chairman Gerald Nathanson. "Nathanson cleaned house when he joined McCrory in 1985. I'm wondering if the same thing isn't happening at Pay 'n Save," said one.

DC, Zimmerman factors

An insider says that Jenkins' frustrations were centered on two interwoven aspects of the Pay 'n Save operation: distribution facilities and Zimmerman-type merchandise.

Pay 'n Save spent $4.4 million during the six months ended May 3, 1986, to upgrade its 350,000-sq.-ft. distribution center. The highly automated

*See **Pay 'n Save**, page 38*

Offbeat convenience for Twin Cities

Will gas/Rx mix for Super America?

MINNEAPOLIS — A new prototype that links a gas station with a pharmacy is lending a new meaning to convenience shopping in the Twin Cities.

Super America, the gas pump and convenience store chain, has installed a pharmacy and drug store merchandise in 3,500 sq. ft. of a 10,000-sq.-ft. prototype that opened in September in nearby Roseville. Two more are under construction in Burnsville and Moundsview. The Ashland Oil subsidiary plans to roll out 10 to 12 such units in the suburbs in the next three years, said Michael Rasnak, the director of pharmacy and manager of H&BA.

Retail industry observers say that no chain in the country has experimented with the gas station-pharmacy combination, and only two convenience store chains have installed pharmacies.

Quick Chek, a convenience store chain in White Horse Station, N.J., and Farm Stores of Edison, N.J., which operates units under the Krauszer's name, both have limited pharmacy rollouts in their convenience stores, retail observers said.

Rasnak said in researching the format he uncovered only a handful of single-store independents who combine the three retailing ventures of convenience store, gas station and pharmacy.

"Prescriptions are a con-

*See **Super America**, page 38*

pharmacy
$6.99

Super America will find out soon if shoppers want to buy gas and pills under one roof. Can pharmacies succeed at gas station-based convenience stores?

FoxMeyer's big new DC signals West Coast push

By Lou Karney

DALLAS — FoxMeyer will make its long-awaited full scale invasion of the West Coast when it opens a 210,000-sq.-ft. distribution center (including 45,000 sq. ft. of mezzanine) in Ontario, 45 miles east of Los Angeles.

The DC will be completed in phases, starting in mid-December, with the final phase set for early February 1987.

What prompted the new DC, which FoxMeyer calls a "supercenter," was the acquisition of Devco Medical Industries in Santa Fe Springs, Calif., in May 1985. Devco, a distributor of hospital supplies, will be fused into the new DC as one of three separate entities. Hospital supplies will occupy 100,000 sq. ft., including Pro-Pac, FoxMeyer's manufacturing division, which makes customized hospital patient kits. Pharmaceuticals and OTC will occupy 45,000 sq. ft., and trucking, 15,000. The rest is for receiv-

*See **FoxMeyer**, page 38*

Eckerd builds Fla. base with SDM buy

CLEARWATER, Fla. — Eckerd is strengthening its presence in many Florida growth markets with its purchase this month of 32 Shoppers Drug Mart stores from Peoples.

The stores correspond in size to Eckerd's 8,000- to 10,000-sq.-ft. format and will build market penetration throughout the state: 18 units in Eckerd's southern and central Hollywood district; nine in the Clearwater, north and central district; and five in the central and eastern Orlando district.

"It's an ideal match for us," said an Eckerd spokesman. He said Eckerd will retain the stores' 480 employees. It will also keep the SDM store names through the Christmas selling season, while adding Eckerd banners.

Eckerd has already shipped its private label products to the stores. Otherwise, the stores "won't be significantly remerchandised," the spokesman said.

*See **Eckerd**, page 38*

Ogiba: Choosing P&G as REX Market Maker
See page 9
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NEWS IN BRIEF

Bergen Brunswig denies charges

ORANGE, Calif. — Bergen Brunswig, the nation's second largest drug wholesaler, has denied allegations made against the company and some directors in a class action suit filed in a California Federal court.

The suit alleges that Bergen violated Federal securities laws in issuing fiscal 1986 financial data.

Bergen's denial called the allegations "speculative and without merit." The company "expects to defend the action vigorously."

Ninth Bud's opens

POTOMAC MILLS, Va. — Peoples Drug has opened its ninth Bud's deep discount store—it's first in this area and the chain's first without a pharmacy.

The store is 36,000 sq. ft., at the upper size range of Bud's. Besides four Bud's in the greater Washington area, the chain also operates in Ohio and Indiana.

Walgreens eyes Twin Cities expansion

MINNEAPOLIS — Walgreens is creating a stir in the Minneapolis-St. Paul market by aiming for 29 units by the end of 1987, up from 24 currently.

The chain broke ground for three additional stores last month, two in downtown Minneapolis and a third in the Coon Rapids suburb.

Walgreens has climbed to about 18% market share in recent years, the second largest slice of the metro pie behind Snyder's Drugs, which has 30% plus, according to retailer estimates here. Since the Twin Cities population has stabilized and created a somewhat flat market, observers expect Walgreens' activity to instigate pricing battles.

A company spokesman said Walgreens will open a total of five new units by the spring of 1987.

Alco Health Services names Kennedy ceo

VALLEY FORGE, Pa. — Alco Health Services has named chairman John H. Kennedy to the additional post of ceo.

Under Kennedy's chairmanship the past 16 months, Alco has grown rapidly, in part through acquisitions, and has virtually tied FoxMeyer in size to become the nation's third largest pharmaceutical wholesaler.

He had been with former parent Alco Standard before joining Alco Health Services.

Durr-Fillauer net, sales up in 3rd qtr.

MONTGOMERY, Ala. — Durr-Fillauer Medical reported gains in revenues and net income during the third quarter and nine month periods ended Sept. 30.

Quarterly revenues rose to $123.7 million, up from $109.4 million in the comparable period a year earlier.

Net income rose similarly in the quarter, to $1.6 million, up from $1.3 million in the same year-ago period.

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Vol. 8, No. 25 November 24, 1986

Perry hires vp-marketing

PONTIAC, Mich. — Perry Drugs has hired its first vp-marketing for its drug store division—a 34-year-old woman with earlier experience as a merchandise manager at Osco Drug.

Betsy Burton, who will report directly to drug division president Mickey Kole, will be responsible for "creating the total market image" for the chain, a company source said. That includes store design, merchandise offerings and presentation, and advertising. The vp's of merchandising and advertising will report to her.

The appointment places Perry among a handful of chains who have developed a strict marketing function.

In the past, Allan Klein, who left Perry more than a year ago, assumed many marketing functions for the drug store segment, while also running the auto parts division.

Burton joined Osco after obtaining an M.B.A. from the University of Chicago. She worked her first two years at store level, then was promoted to merchandise manager for H&BA and appliances.

In 1982, Burton was named president of the Bee Discount subsidiary of Victory Beauty Systems, a wholesale and retail company in the beauty salon industry.

Lucky sells prescription files from 80 closed Gemco stores

Sav-on, Pay Less NW and Longs buy

DUBLIN, Calif. — Lucky Stores revealed to *Drug Store News* how it is disposing of the prescription files in the 80 Gemco stores it will close by year-end.

Of the 80, 26 pharmacy files were sold for undisclosed sums to three chains: 15 to Sav-on, which operates in California, Arizona and Nevada; seven to Pay Less NW in northern California; and four to Longs, including two in southern California and two in northern California.

Another 22 are being transferred to existing pharmacies in Lucky supermarkets, and 26 will be moved to new pharmacy departments to be built inside existing Lucky supermarkets in California.

The fate of the remaining six is still unresolved.

Reasons for Sav-on edge

The Sav-on division of American Stores topped Pay Less and Longs in the numbers for two reasons:

- Sav-on has the most drug stores in southern California except for Thrifty, and when Thrifty declined to bid, Sav-on moved to the inside rail.
- Sav-on is believed to have had an edge because Sam Parker, president of Gemco, was former president of Sav-on.

Meantime, the president of a small southern California independent chain told *Drug Store News* that Lucky "froze us out. I phoned Lucky repeatedly, but they did not return my calls."

A drug wholesale exec evaluated Lucky's actions: "When [Asher] Edelman made his original offer to Lucky, Lucky . . . tried to fight him off with an influx of cash, so they sold Gemco. They didn't want to spend time dickering with independents on each pharmacy file; they sold them in groups because it was faster."

(Following Lucky's rebuff of Edelman's $37-a-share offer, Edelman purchased a 500,000 share block on the open market for $33.50 a share or $16.8 million that raised his holding from 3% to almost 5%, according to a *Wall Street Journal* report.)

Committed to pharmacy

The significance of Lucky's retention of 48 Rx files makes a cogent statement for Lucky's commitment to pharmacy. After the Gemco close-out, Lucky will continue to operate 79 pharmacies in Lucky supermarkets, which average 31,000 sq. ft.

Over the years, Lucky pioneered pharmacy-in-supermarkets and stayed the course, overriding the negative attitude of supermarket shoppers who were uncomfortable having scripts filled in a food store.

But Lucky's persistence paid off. It now does the best job of any supermarket chain in southern California, outpointing Albertson's, Safeway and Vons, market observers said. Vons are aggressive Rx marketers, but Lucky is also price-competitive and has more stores than Vons and more market penetration. Vons has 43 pharmacies in its Value Center and Pavilions combos.

In addition, Lucky has good locations. The result: Lucky fills more scripts than any other supermarket chain—200-300 scripts per day in some pharmacies.

One-stop shopping

Pharmacy is also striking a resonant chord for Lucky in the ongoing movement to one-stop shopping, because Rx offsets to some extent Lucky's tardy move to high-margin service deli, fish and bakery departments.

For more than 25 years, Lucky stayed with everyday low prices. In recent years, however, consumers—especially singles and two-career couples—voted for convenience, and Lucky wasn't moving strongly in that direction.

Rx has served as one of Lucky's first key entries into the one-stop concept.

Wal-Mart fuels dot growth by clustering stores

BENTONVILLE, Ark. — The way Wal-Mart is expanding its dot deep discount drug stores reveals how the retail giant will support the young chain with location and buying synergies among dot, Sam's Wholesale Clubs and Wal-Mart stores.

By opening four dots this year, Wal-Mart has raised its count to six: three in Des Moines, two in Kansas City and one in Wichita, Kan.

Wal-Mart hasn't made final any store growth plans for dot in 1987 or beyond, said Paul Carter, executive vp-special divisions. But the growth pace so far meets earlier stated plans and indicates that Wal-Mart is pleased with performance.

Dot will most likely expand where Wal-Mart or Sam's already operate—not so much for traffic, advertising or distribution efficiencies, but for familiarity. Ads and shipping are typically nonexistent concerns for deep discount drug operators, since ads rarely continue beyond grand openings and nearly all goods are drop-shipped to stores.

By clustering dots in target markets, Wal-Mart will "pick a market and try to dominate it by outstoring in this format," Carter said. That's the same way Wal-Mart has always approached new markets with its discount department stores.

Opportunistic buying

The dot chain will also probably benefit from Sam's ongoing experience in strict opportunistic buying. Carter told *Drug Store News* that "we'd certainly want to take a look at" tacking onto Sam's orders to gain volume discounts. The 100,000-sq.-ft. wholesale clubs sell large volumes of health & beauty aids.

At present, the dot managers order all merchandise for their stores individually, subject to "some centralized review of buying," Carter said.

Dot also has no current plans to test scanning—despite being a heavily sku'd high volume operation. Workers at the 25,000-sq.-ft. stores continue to price-mark all merchandise, Carter said.

That indicates the measured growth program that Wal-Mart apparently has for dot.

In a separate move in pharmacy, the Wal-Mart chain recently surpassed the benchmark of 500 stores with pharmacies, including about 80% company-owned and the rest leased, Carter said.

MERCHANDISING TRENDS

Private label and generic H&BA trends

(% share of $ sales in food stores)

Category	1980	1983	1985	Category	1980	1983	1985
Baby powders	10.31%	12.48%	12.57%	Laxatives	3.04%	3.36%	3.56%
Baby oils, creams, lotions	10.28	16.24	18.00	Synthetic vitamins	30.60	28.03	30.24
Roll-on deodorants	0.65	1.00	1.08	Internal analgesics	2.77	4.00	4.21
First aid products	11.75	15.31	16.80	External analgesics	23.58	25.37	25.64
Hair shampoo	4.35	4.43	3.65	Cough remedies	0.70	1.29	2.29
Hair spray	0.81	1.18	1.41	Cold tablets	1.42	1.50	2.05
Hair conditioning rinses	2.51	3.33	2.41	Razor blades	2.99	5.20	5.41
Toothbrushes	2.93	5.29	4.49	Hand and body cream, lotions	4.45	3.90	3.53
Mouthwash	2.64	3.78	3.97	Facial preparations	0.13	0.69	0.82
Appetite suppressants	—	1.81	1.43	Source: SAMI			

Private label H&BA share reaches 4%

NEW YORK — Private labels and generics accounted for 4% of total health & beauty aids dollar sales in food stores in the year ended July 18, 1986.

That level matched the 1982 peak in this category, reported Selling Areas-Marketing Inc. (SAMI) in a recently released report, *SAMI Analysis of Generic and Private Labels*.

The sales share of nonnational brands in H&BA had dipped to 3.9% in 1983 and to 3.7% in 1984, before stepping back up to 3.9% in 1985.

Still, these levels were well above the 3.3% recorded in 1980.

Increase in share

Today's 4% level represents a 21% increase in share from 1980. In 1980, private label accounted for 3% of the 3.3% nonnational brand H&BA sales in food stores; generics made up the 0.3% remainder. Today, private label accounts for 3.4% of the 4% total; generics, 0.6%, or double its level of six years ago.

The private label and generic gains made in H&BA ran counter to trends in the vast majority of 231 product categories tracked by SAMI since 1980.

After private labels and generics peaked in 1982 at 16.8% of all food store sales, the trend reversed rapidly in virtually all categories. A continuous slide since then caused the private labels/generics share to skid to 13.6% today, the report said.

Private labels took the brunt of the dollar sales slip, sliding from 14.4% in 1982 to 12% currently. Generics fell from a 2.4% share in 1982 to 1.6% currently.

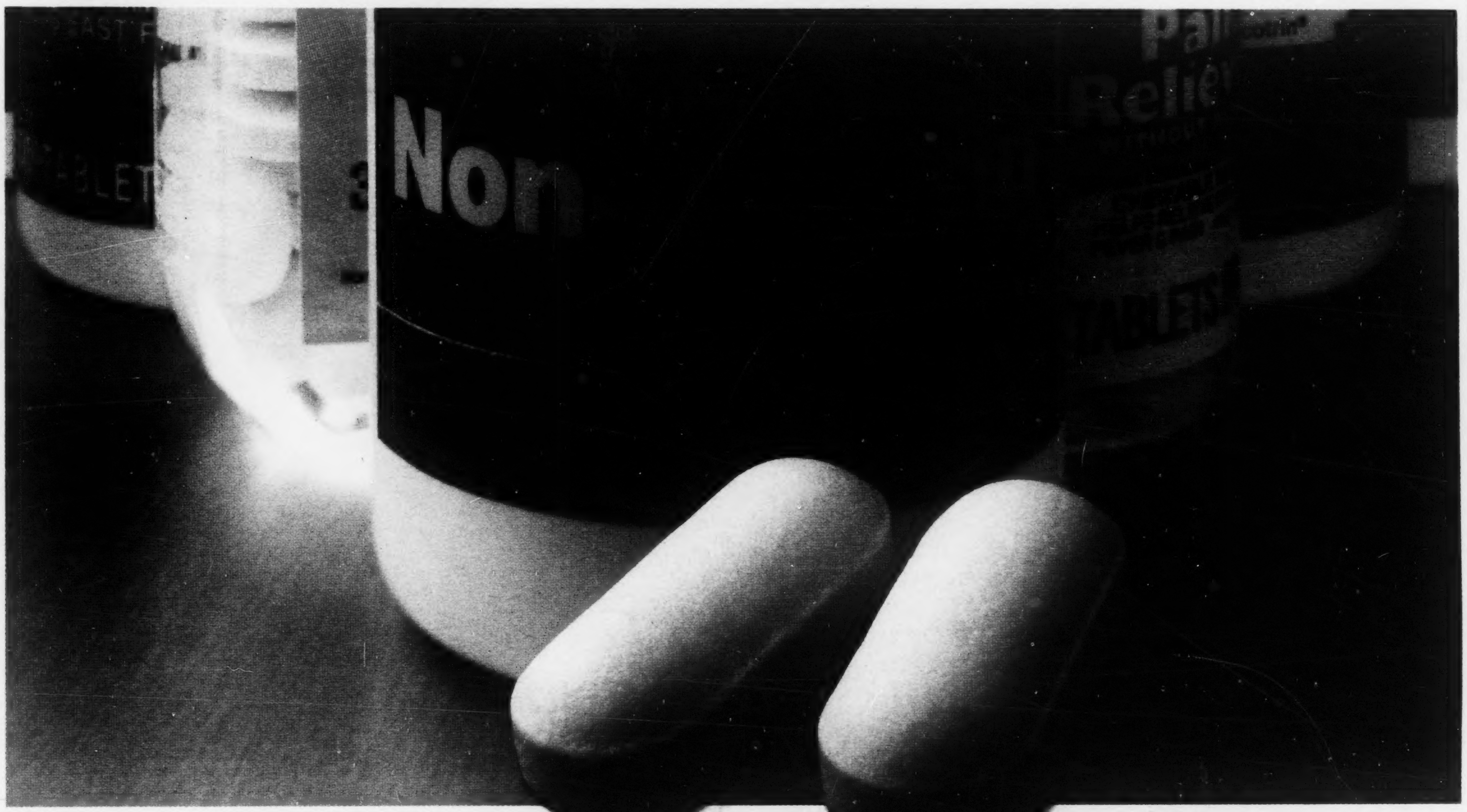
Reasons for decrease

Stating reasons for the slides, Alan B. Miller Jr., SAMI vp-sales services, noted "the easing of inflation in 1983 and ever-increasing issuance of price-off coupons offered by retailers as well as manufacturers. Take away the price advantage and most consumers will choose an advertised brand."

Besides the comeback in H&BA, private label and generic growth appeared in such commodity products as powdered milk, granulated sugar, dog and cat food, coffee filters and paper and plastic plates, the study showed.

Category breakdowns within H&BA show a mixed bag of upturns and downturns between 1982-1985. Among them:

- Baby oils, creams and lotions, up from 14.34% to 18%.
- First aid antiseptics, up from 9.93% to 11.18%.



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We have also added Children's Non-Aspirin Elixir, Children's Chewable Non-Aspirin Tablets, and Extra Strength Sinus Tablets.

Stool Softener Capsules with or without laxative can now also be put on the shelf under the Good Health logo.

And Hygienic Cleansing Pads, which often outsells the National Brand in private label, is now available in Good Health.

Allergy Tablets and Hydrocortisone Cream are also new additions to the line.

We've also updated some package designs and added new sizes, bringing the total number of Good Health products to 81.

And we are now also offering the most exciting addition to your analgesics program in years–Ibuprofen Tablets.

Instead of shopping all over the country to find National Brand alternatives, you can do it in one place, with one order.

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Demographics alter business, execs told

CHICAGO — Demographic changes over the past decade are having a profound effect on today's chain drug store business, as service becomes more important than price.

In a talk given before several hundred chain drug store executives attending the NACDS Administrative/Operations Conference here, Dr. Bickley Townsend, director of the American Demographics Institute, said that today's consumers can be classified as a "two-tier society."

Losers and winners

"There appears to be a move toward a society of economic losers and winners with very little common ground between the two," said Townsend. "There are those consumers making good money with little time to shop and those with time to shop but cash-poor. Because of an increase in two-family incomes and other demographic factors, I believe that we are starting to see, and probably will continue to see, chain drug stores cater more to those individuals who are earning more money with little time to shop."

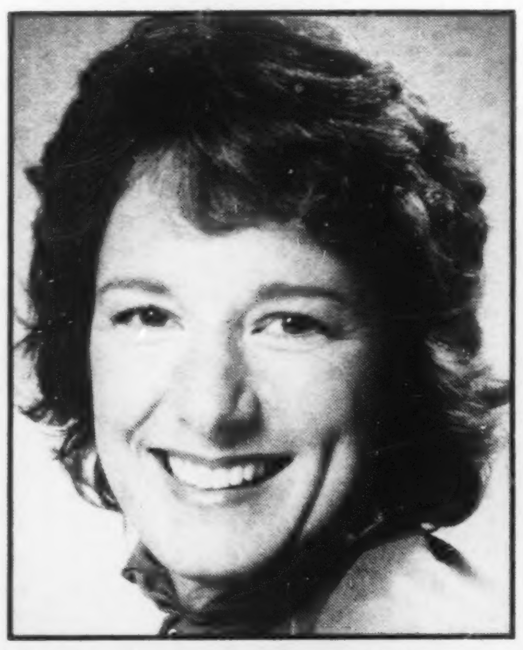
She said this translates into the chain drug store offering increased services.

Townsend cited many factors she believes are responsible for consumers' changing attitudes.

Of primary importance is that the baby boomers have grown up. "The median age of our population has risen from 28 in 1982 to 36 in 1986; therefore, there are more people in the workforce than ever before," she said.

Additionally, Townsend pointed out that there is more

See **Demographics,** *page 28*



'Service is an old-fashioned idea that's coming back in style.'

—**Dr. Bickley Townsend**
American Demographics
Institute

Pay 'n Save Seattle pharmacists settle

SEATTLE — Settlement terms of the seven-week strike of Pay 'n Save pharmacists in Seattle will undoubtedly set the pattern for other Pay 'n Save regions where negotiations with the Guild for Professional Pharmacists are continuing.

These include 40 Pay 'n Save stores in the rest of Washington, 29 Bi-Mart drug stores in Oregon and two Pay 'n Save stores in Idaho.

Two major issues precipitated the strike: wages and sick pay.

Settlement terms

Under the terms of the settlement, staff pharmacists went from $15.90 to $17.50 an hour for three years ending October 1989, and head pharmacists from $16.20 to $18.25 over the same period.

The union's goal was $19.25 (staff) and $19.75 (head) so that Seattle pharmacists would have parity with Portland pharmacists.

A wage-related issue was the retention of overtime after eight hours per day. Pay 'n Save wanted overtime to begin after 40 hours per week. On this issue, the union prevailed.

As for sick leave, the guild first tried to equalize with southern California pharmacists whose contracts (with both the guild and the United Food and Commercial Workers) specify six days per year. Rejected by Pay 'n Save, the guild tried for three days—but came up empty-handed.

The guild also tried for a guaranteed break period during each shift, but was rebuffed. Pay 'n Save has no chainwide policy on breaks, but instead relies on the discretion of each store manager.

Apart from the strike—but with implications for future bargaining—is the breakup of multibargaining by UFCW with major chains. That came

See **Pay 'n Save,** *page 28*

Drug chains back NACDS on modified CIP

WASHINGTON — Chain drug store companies rallied around the National Association of Chain Drug Stores' plan to overhaul Federal Medicaid drug reimbursement rules.

Officials from more than half a dozen major drug chains, as well as several smaller pharmacy operations, detailed their support for the NACDS plan—a variation on the Health Care Financing Administration's pro-generic "Competitive Incentive Program."

Under the NACDS proposal, Medicaid would reimburse drug stores at marketplace prices capped at the 90th percentile for all products supplied by only one or two manufacturers. For drugs available from three or more manufacturers, generics would be reimbursed at full marketplace prices, and brand-name products at "usual and customary" prices capped at the 75th percentile.

Cost savings

"This approach, with the percentile cap, will continue to reinforce competition in the market, providing real program cost savings and positive incentives for providers," said Michael Zagorac Jr., Jack Eckerd Corp. vp-public affairs. "The retail pharmacy marketplace should be at the top of H.C.F.A.'s list to put competition into the Medicaid drug program," he said.

Michael W. Simpson, president of the 10-store Drug-Sav discount chain in Tyler, Tex., echoed Eckerd's emphasis on

See **CIP,** *page 29*

PMA slams all 3 H.C.F.A. Medicaid plans

WASHINGTON — The Pharmaceutical Manufacturers Association and several individual drug companies attacked Federal Medicaid drug reimbursement plans, calling them "cumbersome, unnecessarily complex and vaguely defined."

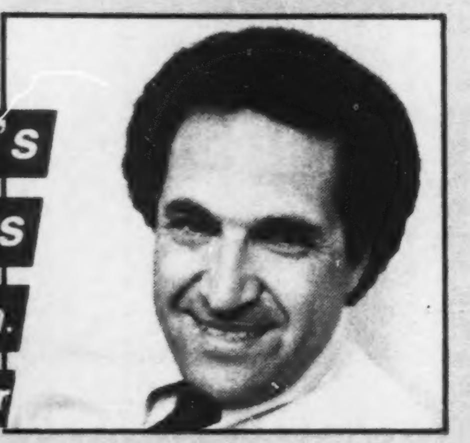
Urging the Health Care Financing Administration to scuttle all three proposals, PMA president Gerald J. Mossinghoff said Medicaid should improve administrative practices and rely on competitive marketplace forces to achieve savings.

"Drug claims under Medicaid represent 8% of the Medicaid budget, but involve an estimated 50% of its red tape and paper-

See **PMA,** *page 28*

Computer exhibits open new vistas for pharmacy

Cohen's
Capsules
Harold Cohen, R.Ph.
Pharmaceutical Editor



I've always been a collector of gadgets, especially of the electronic kind. That's why when computers arrived on the pharmacy scene, I was one of the first to look at them.

Even though those first pharmacy computers had limited memory and took up a lot more space than today's models, for me it was love at first sight. I knew that if I was going to be successful in retail pharmacy, a computer would have to share the limelight. And to think that was a mere five or six years ago.

We've come a long way from the mini-computer with 64K of memory. Most of today's systems pack at least 10 times that memory into a computer cabinet aptly called a "micro," sometimes as much as a quarter the size of the original pharmacy systems. And most operate with the speed of a blinking eye. Even with all of today's sophisticated technology becoming rather commonplace, I'm still impressed with the computer's power every time I use it.

I guess that's why I came away from this year's NACDS Administrative/Operations Conference, recently held in Chicago, shaking my head in amazement over what I saw. If today's pharmacy operation, chain and independent alike, is having trouble competing in its market, it can't be blamed on a lack of technology.

Walking up and down the rows of exhibits, I was drawn to pharmacy computer systems that offered far more than keeping patient profiles and typing labels.

For instance, one system hooked up a voice synthesizer with an automatic dialer. The computer will automatically "look" in its refill files for prescriptions coming up for renewals and call customers to remind them. The best part is that it's done while you are still filling prescriptions.

The system doesn't stop at refills, either. You can actually "program" the computer to call your customers in an orderly fashion (alphabetically, by zip code, etc.) and give them sales messages. Not only is today's pharmacy system a terrific help in filling prescriptions, it has become a first-class marketing tool as well.

Other vendors were showing off high-tech pharmacy software programs that allow pharmacists to price product on their shelves automatically, based on an overall gross profit projection for a particular department while keeping selected products within that department competitive with the marketplace.

And how about those point-of-sale systems with scanning options that hook up the pharmacy computer with electronic cash registers to keep running inventories.

Or how about databases that instantly cross-check patient profiles for drug interactions and possible allergic reactions.

The list goes on and on. And you wonder, what's next? Whatever technology is ahead, I believe it will continue to make the pharmacy profession a better profession for both the pharmacist and the consumer.

PMA rips H.C.F.A. on Medicaid plans

Continued from page 27

work," he charged. "Each of the three proposals can only exacerbate that situation."

H.C.F.A. alternatives under fire include:

- Pharmacists Incentive Program—Payment of 150% of the lowest advertised price plus a dispensing fee for a multisource drug, and payment of the lower of the pharmacist's acquisition price or the "usual and customary" cost plus dispensing fee for a single-source drug.
- Competitive Incentive Program—Payment of the price a pharmacist charges the majority of private retail patients less an arbitrary "pro-generic" discount.
- Revised Maximum Allowable Cost Program—Streamlined version of the current Medicaid drug reimbursement scheme.

According to the pharmaceutical manufacturers, all three plans ignore current marketplace trends, which are already reducing Medicaid prescription drug costs.

Studies cited

Kenneth P. Berkowitz, Hoffman-La Roche assistant vice president, told Federal planners that independent studies funded by the company indicate the H.C.F.A. will exceed its goal of $38 million savings "without undertaking any further regulatory initiatives." According to one study, he said, "market forces" (i.e., an upsurge in generic competition) will reduce Federal and state Medicaid drug costs by $324 million from 1986 through 1990.

In addition, the pharmaceutical manufacturers voiced concerns about promoting generics without sufficient regard to bioequivalence.

'Controversial assumption'

"All three proposals are premised on the controversial assumption of therapeutic interchangeability among generic and pioneer (brand name) drugs, an assumption that the Food and Drug Administration is just now, and rightly, re-examining," said Edgar G. Davis, Eli Lilly vice president.

Industry officials further argued that the H.C.F.A. plans "fly in the face" of the Reagan Administration's "free market goals."

In addition, the Federal rule making will be needlessly burdensome to state agencies that are already developing cost-containment devices, contended Timothy Russell, McNeil Pharmaceutical vice president. Pfizer officials cited Alabama's improved drug claims processing program, designed to save Medicaid more than $51 million in 1987.

Finally, Eli Lilly warned, savings analyses of H.C.F.A.'s plans "did not assess, or even consider," the adverse effect on the public of reduced funds for drug manufacturers' research.

Projected medicaid savings from expanded generic drug availability

	Estimated expenditures	Savings relative to '85 expenditures	
Year	($ millions)	($ millions)	Per cent
1985	$555.37 (Base Year)	—	—
1986	546.99	$ 8.38	1.5%
1987	530.71	24.46	4.4
1988	494.73	60.64	10.9
1989	455.77	99.60	17.9
1990	424.39	130.98	23.6
Total Savings: $324.06			

Prepared by Pracon Incorporated for Hoffman-La Roche Inc.

Pay 'n Save pharmacists in Seattle reach settlement

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about with the NLRB election of April 1986. After that election, Bartell pharmacists voted "nonunion," Fred Meyer remained with UFCW and Pay Less and Pay 'n Save opted for the guild.

"What this has done," said Ralph Vogel, guild president, "is to open competition on pharmacy wages in a region where there is a shortage of pharmacists."

A Pay 'n Save pharmacist in Seattle saw it differently. She said: "Under a single contract, pharmacists are in a better bargaining position because if everyone is on strike, then chains would have trouble filling prescriptions."

Demographics seen affecting chain business

Continued from page 27

household diversity as women enter the workforce in large numbers.

According to Townsend, working, childless couples, because of their full-time jobs, are demanding more service and are willing to pay for it.

"Service is an old-fashioned idea that's coming back in style," said Townsend. "Many working people are willing to trade waiting in lines for service."

Townsend said if retailers are to remain successful, they must pay close attention to these services.

Some of the services consumers are looking for include convenience of location, delivery service and convenient store hours.

"Working couples shop in the late afternoon, early evening and weekends," said Townsend. "Most stores today will stay open late to accommodate them. The ones that don't will lose that business."

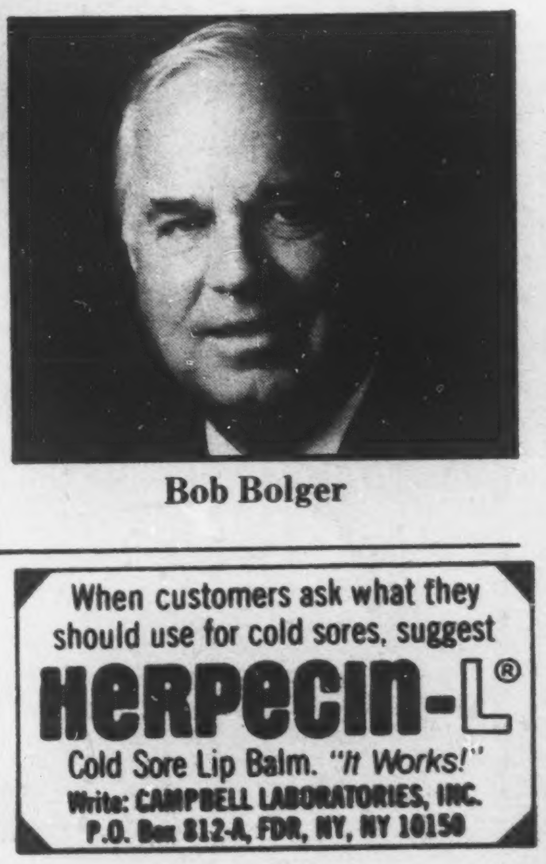
But because of a shift in the labor force, chain drug stores may be hard-pressed to find enough entry-level employees to fill positions needed to boost service, she said.

"Because of the decline in the birth rate in the 60's and 70's, the so-called 'baby bust,' the number of young people entering the job market today is smaller than it was 19 years ago. But the real impact of that baby bust is yet to be felt."

According to Townsend, by 1995, the labor force will have lost some seven million 18- to 24-year-olds.

Commenting on Townsend's presentation, NACDS president Bob Bolger said the chain drug industry must identify their markets and "go after them."

"Not all of [the chain drug stores'] market areas are going to be frequented by customers who are willing to pay for extra service," said Bolger. "Some will fall into the second group of consumers, those that are cash-poor and willing to sacrifice service for discounts. In those markets, the chain drug store will have to give that group what they want as well."



Bob Bolger

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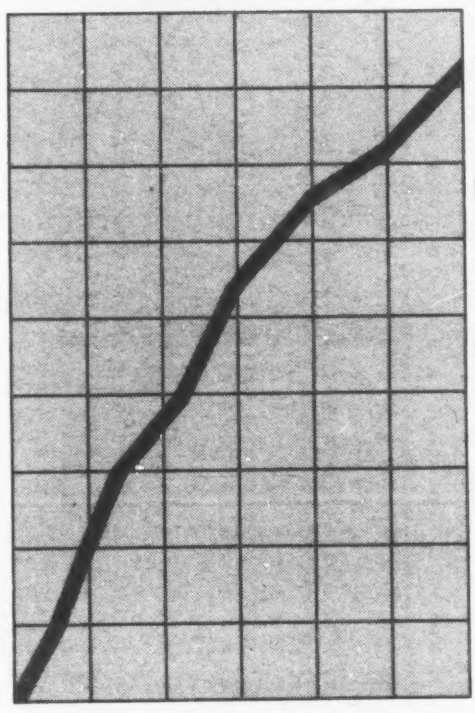

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